

IRS: ENFORCING OBAMACARE'S NEW RULES AND TAXES

HEARING

BEFORE THE

COMMITTEE ON OVERSIGHT
AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED TWELFTH CONGRESS

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Thursday, August 2, 2012,

HOUSE OF REPRESENTATIVES,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, D.C.

The committee met, pursuant to call, at 9:00 a.m. in room 2154, Rayburn House Office Building, Hon. Darrell E. Issa [chairman of the committee] presiding.

Present: Representatives Issa, McHenry, Jordan, Chaffetz, Walberg, Buerkle, Gosar, Labrador, DesJarlais, Gowdy, Kelly, Cummings, Maloney, Norton, Tierney, Connolly, Davis, and Murphy.

Also present: Representative Roe.

Staff Present: Brian Blase, Majority Professional Staff Member; Molly Boyl, Majority Parliamentarian; Lawrence J. Brady, Majority Staff Director; Sharon Casey, Majority Senior Assistant Clerk; John Cuaderes, Majority Deputy Staff Director; Linda Good, Majority Chief Clerk; Christopher Hixon, Majority Deputy Chief Counsel, Oversight; Mark D. Marin, Majority Director of Oversight; Christine Martin, Majority Counsel; Mary Pritchau, Majority Professional Staff Member; Tegan Millspaw, Majority Professional Staff Member; Jeff Solsby, Majority Senior Communications Advisor; Rebecca Watkins, Majority Press Secretary; Kevin Corbin, Minority Deputy Clerk; Yvette Cravins, Minority Counsel; Ashley Atienne, Minority Director of Communications; Susanne Sachsman Grooms, Minority Chief Counsel; Jennifer Hoffman, Minority Press Secretary; Carla Hultberg, Minority Chief Clerk; Una Lee, Minority Counsel; and Suzanne Owen, Minority Health Policy Advisor.

Chairman ISSA. The Committee will come to order.

The Oversight Committee exists to secure two fundamental principles: first, Americans have a right to know that the money Washington takes from them is well spent; and, second, Americans deserve an efficient, effective Government that works for them.

Our duty on the Oversight and Government Reform Committee is to protect these rights. Our solemn responsibility is to hold Government accountable to taxpayers because taxpayers have a right to know what they get from their Government.

Our job is to work tirelessly, in partnership with citizen watchdogs, to deliver the facts to the American people and bring genuine reform to the Federal bureaucracy.

Today we meet because President Obama's health care law, which was hastily written here in the House, so much so that it was once said we have to pass it to find out what's in it, now be-

gins to be implemented. As we implement over 20 new tax laws, the IRS, always willing to say we can do it, it will be difficult, but we can do it, is going to be asked to invade American's lives like never before. Who you are sleeping with, who is in your bedroom, who you are married to or not married to will, in fact, affect your status, and perhaps cause your taxes to be taken retroactively because of a change in income, marital status, persons living within the home during the year.

President Obama said you could keep the health care you wanted, but, of course, that is not happening. It is not happening in such great numbers that States who decided to rely on subsidized, under the Obama health care plan, subsidized health care are being told that involuntarily the Federal Government is setting up exchanges that will, in fact, preempt State's rights, preempt Federalism once again.

Under the letter and the discussion on the House floor of ObamaCare, it was very clear that States could choose whether or not to set up exchanges, and if they did not, Federal exchanges would not be subsidized. It was considered to be an incentive, an incentive that only four States have chosen.

Americans know today that, in fact, this was one of the largest and most complex tax increases in American history. We know that, whether you are a medical device manufacturer finding that you are being taxed so as to raise the cost of health care in order to pay for health care, or whether your dividends and interest are being taxed for the first time ever under Medicare, or whether or not getting married could cost you \$3,400.

The fact is, under ObamaCare if you are making \$25,000, in other words, \$10 an hour with a little bit of overtime, but living unmarried, you will receive about \$1,700 in subsidy. If you live with somebody who also makes \$25,000 and is unmarried, they will get about \$1,700. But if the two of you are foolish enough to get married, you will lose that \$3,400.

The numbers are not debatable. What is debatable is, with rules not yet written on a law that was so vague that time and time again the Administration tells their political appointees to interpret the meaning, to find that which is not within the four squares of the law, and simply say it was Congressional intent.

I am one who was here for that vote. The intent was clear. It was an intent to deceive. ObamaCare was, in fact, a series of promises by Nancy Pelosi to Democrats in order to get them to vote for things that they otherwise wouldn't have. Those Democrats, some of them here, some of them no longer here, have, in greater and greater numbers, realized they were lied to. Whether it was interfering with the churches, interfering with people's personal right to stay with their own insurance company, or, in fact, interfering with Federalism, itself, and States' rights to choose or choose not to participate, time and time again this Administration has broken promises through interpretation.

It has been a long time since this Committee has looked at an IRS Commissioner and had to say what we will say today, which is, Madam Commissioner, you do not have the authority. You simply have the political will to interpret that States must, over their objections, operate effectively State exchanges, because if you don't

do it we will do it for you, and without coming back to the Congress for a change you will cost the American people billions of dollars, hundreds of billions of dollars over ten years, that were not scored in the bill.

Ultimately, ObamaCare, and I am calling it ObamaCare from now on. I am tired of calling it an affordability bill. It is not. It is not about quality health care and it is not about affordability. It was the largest increase in Federal spending and it scored in a way that was not true.

Our primary reason today is to flesh out some of these clear problems, problems where either the law is unclear, or when the law is clear it is chosen to be ignored, or, more importantly, the intrusion by the IRS in our lives.

Under this legislation and its interpretation by political appointees at the IRS, we will see every aspect of the American life audited by the IRS in an increasing way, so much so that I doubt they can, in fact, go after the conventional tax cheat for the next several years.

In closing, I do not blame the IRS. They are just following political orders. I blame the President of the United States for pushing, when he can't get through legislation, implementation of things that were not within the four square.

Treasury and all of its individuals need to recognize that we will hold them accountable for the mistakes and the intrusions into people's lives.

Lastly, for the American people that may be aware of today's hearing, there are many things which people object to in the Census, which comes once every ten years, with follow-ons throughout. The Census will not be nearly as intrusive as the IRS will be under this. States will be receiving information and other individuals, the IRS will be receiving information related to many things that have never been within the four squares of the Internal Revenue Service.

More importantly, portals will be wide open to those who need to know about whether or not you are married, you have a change in employment, and the like, so the opportunity for leaks out of the IRS outside of Federal IRS employees will inherently grow. I am extremely concerned that January 2014 will come and we will have one after another failures to maintain the confidentiality of this new and expanding information.

Lastly, the American people need to understand insurance carriers and exchanges will receive credits based on what the IRS believes should be paid. You may not go to a doctor the entire time. You may, in fact, want no health care. You may be 30 and healthy.

But if your income rises, you marry, or do anything else that might affect that standing, or if the IRS simply overpays, they will not go back to the insurance company who shouldn't have gotten the subsidy; they will go to you and take the money. You will be dunned by the IRS, an organization which can pursue you through bankruptcy, which has no limit to its powers, to eventually collect back money that you may not have wanted to spend.

And, by the way, that \$3,400 on the board and others, your employer will also first be told that he participates under ObamaCare in that subsidy if he doesn't offer health care and you chose an ex-

change, but oh, by the way, it is doubtful whether or not he will get it back as they choose to collect it from somebody who ultimately made more pay than what was possible for the subsidy.

That and so many other questions, so many other dozens of questions, are with us today.

I want to thank our panel, and recognize the Ranking Member for his opening statement.

Mr. CUMMINGS. Good morning.

I have said it to my constituents and I have said it to my family, the 30 years that I have been in public life there is nothing that I have done, no vote that I have cast, that I am more proud of than the Affordable Care Act, and the reason why I say that is because I see the people who it will help and I know that there are people who will die—will die—will die—without it. That is real.

And, as I said to some constituents the other day, if they want me to leave my neighbors on the side of the road sick, unable to get preventive care, like the lady that I met the other day with colon cancer who said, Congressman, just save my life. I have no insurance. Fortunately, we were able to work with her to get her in NIH. Then those are the people who will benefit.

And I will say that, as we address this IRS issue, this is the United States of America. We can do this. We can get this done.

The Affordable Care Act is a landmark achievement that will save huge sums of money for our Nation, while extending health insurance coverage to millions of people. They are the ones that get up early, that get the early bus. They work hard. They give it everything they have got. They are our mothers, our fathers, our friends. They are like Tyrone, the gentleman who lived down the street from me who died, and the last word he said to his wife on his sick bed was, Marie, I have got to get up out of here. I ain't got no insurance.

We are talking about them, our fellow Americans, the ones who send us here.

So last month the Congressional Budget Office issued a report finding that the Affordable Care Act will extend health insurance coverage to 30 million people who do not have it today. They are not collateral damage; they are our people. They are Americans. That is an amazing accomplishment that our Nation should be proud of.

In addition, our constituents are already seeing how the Affordable Care Act is putting money back in their pockets. This week insurance companies are returning to their customers, our constituents, more than \$1 billion in the form of rebates and lower premiums. That is a direct result of the Affordable Care Act.

Just yesterday women in private health insurance plans became eligible for life-saving, preventive health screenings with no copays. This is part of the Affordable Care Act's comprehensive effort to save money by focusing on prevention. These are the women in our lives, our wives, our nieces, our daughters.

It also addresses the historic disparities women face when paying for health care. The Affordable Care Act also has begun to ensure that seniors like my mother, who is 86 years old, have access to preventive care. Young adults have access to insurance on their

parents' plans. And individuals are no longer subject to lifetime limits on their care.

While all of these reforms are being realized now, many significant changes are yet to come. The Internal Revenue Service is the key agency charged with implementing many of the Affordable Care Act's provisions by 2014, including minimum coverage requirements and tax credits for individuals purchasing health insurance on exchanges.

This is a considerable undertaking for the IRS, but we can do this. Experts from the Government Accountability Office, the Inspector General's office, and the National Taxpayer Advocate have reviewed IRS's efforts to date, and they have concluded that the IRS is on the right track to successfully implementing the new law.

For example, GAO issued a report that says, "The IRS generally follows leading practices for implementing such a large program, particularly at the level of individual offices and projects, emphasizing that top leadership has been involved."

In addition, the Inspector General issued a report that says this: "Appropriate plans have been developed to implement tax-related provisions of the ACA using well-established methods for implementing tax legislation."

And in her testimony today Nina Olson, the National Taxpayer Advocate, says this: "Since ACA enactment, the IRS has been working through the major challenges, making significant progress. The lead time provided by the ACA has been very helpful for the IRS, and at this point it appears the IRS has used the time well."

Certainly there are significant challenges in implementing this law, and as IRS moves forward it benefits greatly from the continued rigorous oversight and recommendations from GAO, the IG, and the National Taxpayer Advocate. At the same time, we recognize that the IRS has been actively planning to implement the Affordable Care Act for more than two years, and it has already implemented many of the provisions successfully.

For the challenges that remain, the IRS is working closely with taxpayers, the business community, and the insurance industry to ensure that its policies are responsive to consumers and consistent with the intent of Congress in passing the law. I remind us that this is the law.

Today the Committee is faced with a choice: do we act constructively or destructively? Do we build up or tear down? Do we help or do we hurt?

On one hand, we could work with the IRS and its oversight entities to ensure that the Affordable Care Act is successfully implemented, particularly now that the Supreme Court has ruled that it is Constitutional. On the other hand, we could try to exploit any and all ways to bring down this law or starve the IRS out of resources it needs to do its job.

I personally hope that we pursue the first approach; however, Republicans have introduced legislation to do the second. The Congressional Budget Office has examined the Republican bill to repeal the Affordable Care Act and concluded that it would increase the Federal budget deficit by \$109 billion over the next ten years.

It is time to accept the Affordable Care Act, to accept the Supreme Court decision, and to accept the billions of dollars in savings this law will bring to our citizens.

I look forward to today's testimony and I want to thank all of our witnesses for being here today.

Mr. Chairman, I yield back.

Chairman ISSA. I thank the gentleman.

We now recognize Dr. DesJarlais for an opening statement and a unanimous consent.

Dr. DESJARLAIS. Thank you, Mr. Chairman.

Chairman Issa and Ranking Member Cummings, I appreciate your holding today's hearing to further examine how the Internal Revenue Service has been implementing provisions of the Affordable Care Act. One of our chief responsibilities on this Committee is to ensure that taxpayer dollars are being utilized both efficiently and in accordance with the law. Unfortunately, it has become undeniably evident that the Affordable Care Act falls short on both of these principles.

Just last week this Committee held a hearing on a new Health and Human Services demonstration project that the Obama Administration is paying for by cutting \$8 billion from Medicare Advantage. These are funds that would normally be used for patient care. Two members from the nonpartisan Government Accountability Office stated that this demonstration project was unprecedented, flawed from its inception, and will ultimately demonstrate nothing.

Further, there is strong evidence to suggest that the sole purpose of this project was nothing more than an attempt by this Administration to hide new costs that ObamaCare imposes on seniors until after the election. I fail to see how this is an efficient use of taxpayer dollars.

There are the sort of examples that we have come to expect from this haphazardly passed bill authored by individuals who told the American people that they would have to pass it in order to find out what was in it. Well, today I want to focus on what is not in it.

We have now discovered that when the Democrats were drafting ObamaCare they left out important language relating to Federally run insurance exchanges. Democrats wrongly assumed that the States would rush to set up exchanges once the bill was signed into law, but a majority of them are still yet to do so.

Section 1321 of the bill gives authority to the Federal Government to set up exchanges in States that fail to do so on their own; however, the law only gives State-run exchanges the ability to issue premium assistance or tax credits. Nowhere does the bill grant this authority to Federal-run exchanges.

The Obama Administration and proponents of this rule have stated that this was a simple drafting error. I don't see how they can possibly make this claim when Democrats had ample opportunity throughout the reconciliation process where they specifically extended tax credits to exchanges created by U.S. territories, yet left Federal exchanges alone. This leads me to believe that this was, in fact, a deliberate and premeditated action on the part of

the Democrats as a way to incentivize States to set up the exchanges.

Either way, there is no doubt that the language is missing. In order to fix this glaring problem, the Internal Revenue Service circumvented Congress' legislative authority by issuing a rule allowing premium assistance subsidies to be offered through Federal exchanges. Back in November of 2011, my colleague and fellow Tennessee physician, Phil Roe, and I sent a letter to the IRS Commissioner asking what authority his agency had to unilaterally alter the Affordable Care Act and what specifically within the bill gave them the authority to bypass Congress in promulgating this rule. The response we received from the IRS cited no specific section or language justifying their actions.

Mr. Chairman, I ask unanimous consent that this letter and the IRS's response be submitted into the record.

Chairman ISSA. Without objection, so ordered.

Dr. DESJARLAIS. On June 18th I introduced H.J. Res. 112 which would nullify this rule under the Congressional Review Act. I firmly believe the actions by the IRS set a dangerous precedent that flies in the face of our Constitutional separation of powers. I am pleased to announce that Senator Ron Johnson has recently introduced companion legislation in the Senate. Ultimately, my bill and this issue are not about the merits of the President's health care law but on how the IRS has overstepped the authority it was given as a result of the Affordable Care Act.

While my colleagues on the other side of the aisle may not share my views regarding the detrimental affects that ObamaCare will have on our Country, surely they will agree that the framers of our Constitution were clear in giving Congress sole legislative authority. Just because Democrats hastily drafted their health care law due to electoral politics, it doesn't mean they can now throw the separation of powers out the window.

I look forward to hearing the testimony presented before us today, as well as having the opportunity to question our witnesses on these very important issues.

I yield back the balance of my time.

Chairman ISSA. I thank the gentleman.

Members may have seven days in which to submit opening statements for the record.

We will now recognize our panel. We welcome our witnesses on the first panel.

Mr. Mark Everson was Commissioner of the IRS from 2003 to 2007 and is currently vice chairman of the AlliantGroup. I might note, also one of the architects of Governor Mitch Daniels' changes in Indiana. Ms. Nina Olson is currently the National Taxpayer Advocate at the IRS. Mr. Timothy Jost is professor at Washington and Lee University School of Law. And Mr. Michael Cannon is Director of Health Policies at the Cato Institute.

Lady and gentlemen, pursuant to the rules of the Committee, would you please rise to take the oath and raise your right hands.

Do you solemnly swear or affirm that the testimony you are about to give will be the truth, the whole truth?

[Witnesses respond in the affirmative.]

Chairman ISSA. Please be seated. Let the record indicate all witnesses answered in the affirmative.

As is the tradition of my predecessor, I will note that you have a time and lights, so I would only ask that you deal with it just the way you would green light, drive through; yellow light, drive through faster so you don't get caught on the red; red light, please do a final summary as you see your time has expired.

Your entire opening statements will be placed in the record, so you need not go verbatim. It will all be there.

Mr. Everson?

WITNESS STATEMENTS

STATEMENT OF MARK EVERSON

Mr. EVERSON. Good morning, Mr. Chairman, Mr. Cummings, members of the Committee. I am pleased to be here.

As you have indicated, I am the Vice Chairman of AlliantGroup. I want to stress that my remarks are my own, not those of that business. But I would say that we work with CPA firms around the Country, and some of the reflections I am going to make are really tied to things that I have been told.

I would also say that I am not here to advocate for or against repeal of the act or of any specific components of the act. I am trying to help you grapple with this issue of the IRS and its implementation.

As the GAO has noted, this is a massive undertaking. That is the wording they have used. Very significant for the service. Nina Olson, my colleague, former colleague and the National Taxpayer Advocate, has said with proper planning and funding the IRS is fully capable of implementing health care reform. I am not so sure.

Now, clearly I know that the Service is going to do everything it can to implement it. They always do. But this is really quite a heavy lift, if you will.

There are really two questions. One, can they do it, and even if they are able to do it will there be collateral damage to tax administration as they are working on this set of issues. They are both important questions.

The Service grapples with three things when it is implementing laws. Are there adequate lead times? I think there are generally in this act. Is there adequate funding? That is essential if they are to do their job. I counsel you to make sure you provide the funding that they need. And then, finally, complexity. There is a lot of complexity and ambiguity in statutes, and that is certainly the case here.

As Nina has said, complexity is the most serious problem confronting taxpayers, and clearly this is a step backward for tax administration because of what the IG has said is the introduction of the most complexity in over 20 years to the tax code. So that is a big problem.

In my testimony which you have I have raised a number of issues. Let me just mention a few.

The first is information technology. This is going to be a real challenge for the Service. And, as you have indicated, reliance on a lot of outside parties will be the case. You don't have to go any

further than today's news, reading about millions of trades on the stock exchange going forward because of rogue programs or bad programs to know that errors get made. Systems issues are tough. A lot of challenges for the Service here because of the need to constantly update information. This is going to be a challenge.

The second piece you have already mentioned, Mr. Chairman, is the protection of taxpayer data. If there was anything I really worried about as Commissioner, that was it. And there is a risk here that there can be disgorged information, and it would be very damaging to the Service and the confidence of taxpayers in the IRS if that were to happen.

The other point that I would make is the burden on CPAs. CPAs struggle as it is to keep up with all of the changes in the tax code. They are the true advisors to small and mid-sized businesses. They don't have the staffs of the Merc or a GE to work through all this, and this is going to be very challenging. We get a lot of feedback on this at AlliantGroup.

Before I close, I have got three very general points that I think are very important to place this in the overall context.

Health care reform comes at a very difficult time for the IRS. In part, it is Congress' doing. We are heading towards the end of the year where there is a great deal of ambiguity about what the law is. I really do encourage you to resolve these issues, because American businesses need certainty to make investment planning. But beyond that, I think the IRS is looking at the most difficult filing season next year, 2013, that it has had in decades because of the convergence of these factors and the potential for tax reform.

So the competition for resources at the Service and of management attention, they only have so many senior managers, of course, this all comes at a very difficult time.

A second point I would make that I think is sort of over-arching is the independence of the Service. For important and well-understood reasons, the IRS operates with a great deal of independence from other agencies. I worry that such direct participation of the Service in a major non-tax Administration initiative has the potential to erode the historic independence of the Service.

And let me be clear here. I have nothing but the highest regard for Commissioner Shulman and his team. I am not suggesting I have seen things, but I just think that when you bring the Service in closer to the White House and to other agencies you just run the risk of eroding that independence.

Let me conclude by touching on the politics of this and how it does impact the Service. I would say that, with the Supreme Court decision and the clear transfer of looking at all this back into the political arms of Government, it is also clear the Service is coming under attack. It would appear that some opponents of the Reform Act will demonize the IRS in order to build a case for overturning the law.

The most striking example is the disturbing comparison of the IRS to the Gestapo by the incendiary Governor of Maine, Paul LaPage. Reuters quotes LaPage as having said, "What I am trying to say is the Holocaust was a horrific crime against humanity and, frankly, I would never want to see that repeated. Maybe the IRS is not quite as bad yet."

Attacks upon the IRS of this kind are unconscionable and will ultimately take their toll on the Service, its people, and the ability of the IRS to collect the money that we need to fund the Government.

I would close by saying that I would suggest that, even if the Service is successful in executing the long list of tasks assigned to the IRS under the Affordable Care Act, there is still an unquantifiable real risk that health care reform will falter or perhaps, and nobody can be sure of this, but perhaps even fail because of the sheer number of moving parts and complexity of the new system.

Let's hope health care reform is not a modern day version of the Vasa, the famous top-heavy Swedish war ship built in 1628 and when it sailed out of Stockholm harbor it sank 400 feet from shore. If something like that happens because of all the complexity and all the interactions and all these pieces, if that happens, as you say, just two short years from now, the damage to the IRS and the impact on our Country in that regard, not the health side, will be real and lasting.

Thank you.

[Prepared statement of Mr. Everson follows:]

House Committee on Oversight and Government Reform

Statement of Mark W. Everson

Vice-Chairman of alliantgroup, L.P. and former IRS Commissioner (2003-2007)

August 2, 2012

Good morning Chairman Issa, Ranking Member Cummings and members of the House Committee on Oversight and Government Reform. I am pleased to testify before the committee on the challenges facing the IRS in implementing healthcare reform. My name is Mark W. Everson and I served as commissioner of internal revenue from May 2003 through May 2007. I am currently Vice-Chairman of alliantgroup, L.P., a provider of specialty tax services for small and medium-sized businesses. The views I will express today are my own, and not those of alliantgroup, although I would note that some of the concerns I have about healthcare reform arise from conversations with the many CPAs alliantgroup works with across the country.

Introduction

Let me state from the outset that I do not consider myself an expert on healthcare. Nor am I here to advocate for or against repeal of the law or of any of its component parts. That having been said, it is clear to all observers that the IRS faces significant challenges in executing its assigned responsibilities under the Patient Protection and Affordable Care Act ("Affordable Care Act"). The Government Accountability Office has called the work facing the IRS "a massive undertaking." In my testimony I will touch on specific areas of concern pertaining to certain major provisions of the new law, and offer my thoughts on the broader risks to tax administration brought about by housing so much of the reform apparatus within the IRS.

The National Taxpayer Advocate has said that "With proper planning and funding, the IRS is fully capable of implementing healthcare reform." I am not so sure. Certainly I know from my own experience at the IRS that the service does its level

best when asked to take on new duties by Congress. I am confident it is doing just that right now, and will continue to do so over the next several years as it strives to implement the Affordable Care Act. But what the IRS is being asked to take on is really quite staggering. As one senior official not given to exaggerate said to me recently, "It will be a heavy lift." Further, given the complexities of the provisions and the number of parties involved in making the system operate, it is not clear to me that the statutory scheme enacted into law is workable mechanically, even given Herculean efforts by the IRS and others. But whether or not the IRS is successful in implementing healthcare reform, there is a second and equally important question: will tax administration be damaged in the process?

Challenges Facing the IRS in Implementing the Affordable Care Act

When the IRS implements new legislation it typically faces three broad challenges: meeting statutory deadlines; resource constraints; and interpreting complicated statutory provisions and adjusting operations accordingly. Let me comment on these issues before turning to specific concerns. I believe Congress has on the whole provided reasonable timelines for implementing the Affordable Care Act. The major provisions of the new law phase in over a number of years, affording the service the chance to plan its activities and to address both policies and procedures. As to resources, it is of course critical that the IRS have adequate staff and operating funds to make the many systems and operational changes required by healthcare reform. This is a subject of ongoing inquiry by the Congress, and is not the focus of my testimony.

As we know all too well, complexity is an enduring and unfortunate feature of the tax code, and something with which the IRS deals on a regular basis. Nevertheless, complexity permeates the Affordable Care Act and will prove daunting to even the IRS. I would add that complexity associated with healthcare reform will also pose difficulties for taxpayers, both businesses and individuals, and for tax practitioners who will be called upon to help their clients understand and meet new obligations under the law. The National Taxpayer Advocate has cited complexity of the tax code as the "most serious problem" facing taxpayers.

The Affordable Care Act certainly makes this problem worse, damaging tax administration as a whole.

I have a number of specific concerns relating to IRS implementation of the Affordable Care Act. Many of these issues have been raised by others and I would note that the list is non-exhaustive. The following simply strike me as the most important:

Major Systems/Information Technology Requirements:

The IRS collects a vast amount of data and could not execute its tax administration duties without successful operation of the many major information systems upon which it relies. A large number of these systems require constant updating because of unrelenting changes to the tax code. Meeting its ongoing obligations in the systems domain is essential for the IRS, and has grown ever more difficult in recent years with the sharp growth of identity theft. Healthcare reform cannot help but compete with the service's almost overwhelming, regular systems workload. The Affordable Care Act will confront the IRS with the need to collect new kinds of information and to interact with many additional parties. Some of those parties, like the exchanges, will be newly established entities, further complicating the task of modifying existing systems and developing new ones. In several areas the new law will require more or less constant updating of information pertaining to an individual's circumstances. Much of the data capture and analysis performed by the IRS allows the service time to cleanse and match data before using it to determine tax liability, a grace period which the new law in several areas will not allow. Taken together, the systems and IT challenges facing the IRS in implementing healthcare reform pose great risk.

Data Security and Protection of Taxpayer Information:

If there was any one thing that kept me up at night when I served as commissioner, it was the worry that the IRS would belch forth the personally identifiable information of millions of Americans, either through our own error or by having our systems compromised by others. Protection of taxpayer

information is a priority at the IRS from top to bottom, and depends both on the integrity of its systems and the actions of individual parties. The IRS enters into strict protocols with states and other taxing authorities before sharing taxpayer information. Under the new law, the IRS will be sharing taxpayer information with any number of additional parties, many of which will be going through growing pains of their own as noted above. A significant data breach, even if caused by others, would shake America's faith in the IRS and could be catastrophic for tax administration and revenue collection.

Assumption by the IRS of the Obligation to Establish Benefits Eligibility:

Our system of voluntary compliance obligates taxpayers to compile information and report data on their tax return in order to fix a tax liability. Much of this data is later matched with third party reporting information to verify its accuracy. Under healthcare reform, eligibility for advance payments of the premium assistance tax credit or cost sharing reductions will be determined largely from information supplied by the IRS rather than in an application from the individual seeking the benefit. This is an important shift in responsibility. When Exchanges inform an individual that they are ineligible for a benefit to which they think they are entitled because of information from the IRS, there will be a great deal of confusion.

The New Concept of Household Income:

Household income—defined under the Affordable Care Act to include the income of dependents and not just the taxpayer—is a factor in determining an individual's eligibility for the premium assistance tax credit or appropriate cost sharing reduction. This is also a significant departure from existing standards for assessment of tax under the tax code, where household income is nowhere to be found. This change cannot help but further complicate tax compliance, cause confusion and burden the IRS.

Fragmented Responsibility and Authority for Operations; Potential Uneven Application of the Law:

In addition to my service as commissioner of internal revenue, during the Reagan Administration I was Deputy Commissioner of the INS, where I oversaw implementation of the Immigration Reform and Control Act of 1986. Both the Immigration and Nationality Act and the Internal Revenue Code are complicated statutory schemes, making the INS (now part of the Department of Homeland Security) and the IRS difficult to manage. However, one advantage in each organization was a clear chain of command and fixed responsibility for execution of the law. I consider the IRS steady and reliable, but hardly agile. In implementing healthcare reform, the IRS will be highly reliant on other governmental entities and external partners, compounding management challenges. The fragmentation of operational workload increases the difficulty of execution, and will require an extraordinary amount of coordination with other players in the healthcare system on the part of the service.

An objective of tax administration is consistent application of the law—that is, similarly situated taxpayers should get the same answer whether filing in Newark or in Seattle. It doesn't always work out that way, but that is the standard, at least since 1998 when the IRS was reorganized along functional lines (individual taxpayers, small businesses, large businesses and tax exempt entities) rather than geographic lines. The Affordable Care Act grants significant operational and policy waiver authority to the Exchanges, which will put the IRS in the difficult position of explaining the application of differing policies across the country under a single federal statute.

The Reconciliation Process Associated with the Premium Assistance Tax Credit:

This provision has been widely commented upon. I agree with those who have voiced concerns that this particular facet of healthcare reform will cause a great deal of consternation for taxpayers and problems for the IRS because of the statutory construction of the benefit—based on prior year return information--and its potential, but unanticipated recapture from the taxpayer if his or her circumstances have changed and repayment of the credit is required down the road.

The Introduction of Complexity in Their Dealings with the IRS to Many Taxpayers who File Simple, Refund Returns:

While it is true that the tax code is extremely complex, that is not the case for the majority of filers, who do not itemize their deductions or have complex financial transactions to report. Still, these filers of often relatively simple returns will experience the greatest impact of the complex standards of the Affordable Care Act because of their income levels or the fact that they are more likely to not have health insurance. In addition, the IRS will find itself in the middle between employers and employees, obligated to explain information supplied by the other party.

The Impact of Specific Limitations on IRS Enforcement Mechanisms:

Under the new law, the IRS can only enforce penalties associated with the individual mandate through refund offsets, and is prohibited from employing liens or levies, traditional enforcement tools. Variability in procedures increases the risk of inefficiency or error in any operation, the IRS included.

Issues Associated with Improper Classification of Employees:

The IRS has struggled for years to prevent improper classification of individuals as contractors by employers, rather than as employees, in order to avoid employment taxes. Because employers are subject to different obligations under the Affordable Care Act based on the size of their workforce, in all likelihood this problem will grow in magnitude because of the new statute, with implications not just for compliance with the healthcare law, but also for employment and tax laws more generally.

Increased Burden on CPAs:

The United States enjoys a high level of compliance with its tax laws when compared with other nations. To achieve this favorable result, the tax system depends not only on the integrity of taxpayers and the efforts of the IRS, but also on private practitioners, the attorneys and accountants who to a very real degree serve as the arms and legs of the tax system. Tax practitioners not only help

individuals and businesses understand their tax obligations, but also often serve as general financial advisors helping clients navigate government regulations of all sorts. This is especially true for the small and medium-sized businesses which employ two thirds of all private sector workers, and don't have sophisticated tax and human resources staffs poised to explain the intricacies of healthcare reform. The sheer volume of changes associated with the Affordable Care Act, as well as the nature and complexity of certain of its provisions, will be tough for practitioners to absorb, increasing stress across the tax system as a whole. At this stage, CPAs and small and medium-sized businesses are perhaps best described as flummoxed by the Affordable Care Act. This is a problem which is magnified by the disgust and near panic gripping CPAs arising from the inability of Congress to successfully resolve tax matters critical to business, and the failure to provide even a modest amount of certainty for investment planning.

Additional Points Concerning the Impact of Healthcare Reform on Tax Administration

Before concluding, there are three additional points which I think are integral to gauging the potential impact of the Affordable Care Act upon the IRS:

Healthcare Reform Comes at a Difficult Moment for the IRS:

1985 was the last time the IRS failed to deliver a successful filing season and get refunds out on a timely basis, now a distant memory. The 2013 filing season will almost surely be the greatest challenge to the IRS since that date because of delayed congressional action on numerous tax provisions. The rapidly increasing problem of identity theft will greatly compound the task. Tax reform may also draw much of the service's attention next year if it advances and becomes a serious possibility. Even a large organization like the IRS has a limited number of senior executives capable of directing major activities. To the extent that healthcare absorbs their time, tax administration will suffer.

Independence of the Service:

For important and well understood reasons, the IRS operates with a great deal of independence, both from other government agencies and the White House itself.

Even though I had served in the Executive Office of the President as Deputy Director for Management of OMB, I felt in some ways as though I had moved to Siberia when I began my appointment as commissioner. They even dropped me off the Bush White House Christmas party list! I can only recall one meeting in four years where I participated in a discussion with White House staff and officials of other agencies covering a policy matter. I was there to explain limitations on the use of taxpayer information in connection with establishing work eligibility, part of the discussion of potential immigration reform.

I worry that such direct participation of the service in a major non-tax, administration initiative has the potential to erode the historic independence of the IRS. Let me stress that I have every faith in the integrity and leadership of Commissioner Shulman and the members of his team, and that I am unaware of specific problems arising from the regulatory or implementation process. It is also true that the IRS has engaged in interagency collaboration in the past under certain important pieces of legislation, most notably ERISA. Nevertheless, I fear that the IRS is on a slippery slope as regards its traditional independence due to being so intertwined with a major domestic policy initiative like healthcare reform.

Insertion of the IRS into Political Discourse:

The recent Supreme Court decision upholding the centerpiece of the Affordable Care Act based on the taxing powers of Congress has shifted debate over the merits of the legislation back into the political process. Unfortunately, it would appear that some opponents of the reform act will demonize the IRS in order to build a case for overturning the law. The most striking example is the disturbing comparison of the IRS to the Gestapo by the incendiary governor of Maine, Paul LePage. Reuters quotes LePage as having said, "What I am trying to say is the Holocaust was a horrific crime against humanity and, frankly, I would never want to see that repeated. Maybe the IRS is not quite as bad—yet." Attacks upon the IRS of this kind are unconscionable and will ultimately take their toll on the service, its people, and the ability of the IRS to collect the revenue which largely funds our government. The IRS did draw down its enforcement activities in the

late 90's and early in the last decade after a savaging in the political arena. The country could afford it then. We were running budget surpluses. Now we need the money.

I have raised a number of concerns regarding healthcare implementation by the IRS. There are of course others. I would suggest that even if the service is successful in executing the long list of tasks assigned to the IRS under the Affordable Care Act, there is still an unquantifiable but real risk that healthcare reform will falter or perhaps even fail because of the sheer number of moving parts and complexity of the new system. Let's hope healthcare reform is not a modern day version of the *Vasa*, the top heavy Swedish warship which in 1628 sank minutes into its maiden voyage, less than 400 feet from shore. The damage to tax administration of any such failure would be serious and long term.

Thank you.

Chairman ISSA. Thank you.

This Committee did research a Coast Guard ship that will crack in two in less than its first 20 years, so we are not completely beyond that at this time.

Ms. Olson?

STATEMENT OF NINA OLSON

Ms. OLSON. Chairman Issa, Ranking Member Cummings, and members of the Committee, thank you for inviting me to testify today about the IRS's implementation about the Patient Protection and Affordable Care Act.

As you know, my office is non-partisan, so I take no position pro or con regarding the wisdom of the ACA; rather, my focus has been and continues to be on trying to ensure that a taxpayer perspective is considered as the IRS prepares to implement the law as it stands today.

In my 2010 annual report to Congress, I published a detailed assessment of the administrative challenges the IRS will face in implementing the four major tax provisions of the law. Since that time, my office has monitored the IRS's preparations for the ACA closely. Overall, I believe the IRS has done a good job of moving quickly to identify its key challenges, and has taken significant steps to address them, although some concerns remain.

On the positive side, the IRS has already issued considerable guidance to clarify gray areas of the law. I view the early publication of guidance as a very positive development, because it enables both taxpayers and employers to know where they stand and to make informed decision about their coverage options, and also to allow others to litigate against those State-taken positions.

The IRS also has made progress in developing business requirements for computers and other information technology. IT infrastructure lies at the core of the IRS's ability to administer the program, largely because the IRS will use computer systems to communicate with the exchanges. Early systems development will allow for repeated advanced testing and enable the IRS to identify and fix glitches before the systems go live.

My own organization, the Taxpayer Advocate Service, or TAS, has also been making preparations, including initial training of our employees on key provisions of the ACA, reviewing and commenting on drafts of published guidance, designing an online tool to help small businesses estimate the amount of small business health care tax credit they may receive, and conducting a survey of individuals and businesses regarding health insurance coverage and needs that will provide useful demographic information for outreach purposes.

Notwithstanding these important steps, some areas of concern remain. First, the IRS and other entities need to step up their public information campaign. The IRS should make it a top priority to work with other agencies to develop and deploy a targeted communications campaign designed to anticipate and answer questions from individuals and employers. As part of this campaign, the IRS should educate taxpayers who receive the advance premium tax credit about the importance of updating information if their income or other relevant circumstances change. If the taxpayer continues

to receive a subsidy but becomes ineligible, he or she will end up with an unexpected tax bill when eventually filing the related return.

Most taxpayers otherwise are not required to provide periodic updates to the IRS, so this new procedure needs to be communicated clearly.

Other remaining challenges include establishing smooth inter-agency communications, minimizing the impact of tax-related identity theft on eligibility determinations, and providing additional guidance for small businesses and employers.

I also believe it is critical that the IRS begin to include representatives of my office on its implementation teams. Congress placed TAS within the IRS specifically to ensure that the IRS considers our taxpayer perspective as it develops and implements programs, and with any program the devil is in the details, and if TAS representatives are not included on the teams where the details are hashed out, I am concerned the taxpayers eventually will be harmed.

On the whole I believe the IRS will be able to successfully implement its responsibilities under the ACA, but I believe it is critical that the IRS receive adequate funding to meet taxpayer needs. If the funding is restricted, the IRS simply cannot cut spending on ACA implementation, because unless Congress changes the law, administering the ACA is a statutory requirement. Rather, the IRS would have to make cuts in its taxpayer service and enforcement programs, and that would be a mistake.

In my 2011 annual report to Congress I identified the combination of the IRS's expanding workload and its shrinking resources as the number one most serious problem facing taxpayers. I am deeply concerned that taxpayer service suffers the most when IRS funding is inadequate, and I therefore urge you to ensure that U.S. individuals and businesses that are trying to pay their taxes and are seeking help from the IRS are not shortchanged.

Thank you for letting me testify today, and I would be happy to answer your questions.

[Prepared statement of Ms. Olson follows:]

Chairman Issa, Ranking Member Cummings, and distinguished Members of the Committee:

Thank you for inviting me to testify today about the IRS's implementation of the Patient Protection and Affordable Care Act (ACA).¹ This testimony will make the following points:²

1. Since publishing a 2010 study on the challenges posed by the law, the National Taxpayer Advocate has been closely monitoring IRS implementation of the ACA.³
2. The IRS has made significant progress toward ACA implementation.
3. The Taxpayer Advocate Service (TAS) has participated in ACA preparation.
4. There remain significant concerns with respect to ACA implementation.

Two notes of introduction to my testimony:

First: Since I generally report to the House Ways and Means and Senate Finance committees, I would like to briefly explain the statutory authority and role of my office. Congress created the position of the National Taxpayer Advocate and the Office of the Taxpayer Advocate (also known as the Taxpayer Advocate Service, or TAS) to assist taxpayers in resolving their problems with the IRS, to identify problems affecting groups of taxpayers, and to propose administrative and legislative recommendations to mitigate those problems. The National Taxpayer Advocate is appointed by the Secretary of the Treasury and reports directly to the Commissioner of Internal Revenue but is required to provide an independent perspective as the statutory "voice of the taxpayer" both within the IRS and by submitting two reports each year directly to the congressional tax-writing committees.⁴

¹ Pub. L. No. 111-148, 124 Stat. 119 (2010), amended by the Health Care & Educ'n Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010).

² The views expressed herein are solely those of the National Taxpayer Advocate. The National Taxpayer Advocate is appointed by the Secretary of the Treasury and reports to the Commissioner of Internal Revenue. However, the National Taxpayer Advocate presents an independent taxpayer perspective that does not necessarily reflect the position of the IRS, the Treasury Department, or the Office of Management and Budget. Congressional testimony requested from the National Taxpayer Advocate is not submitted to the IRS, the Treasury Department, or the Office of Management and Budget for prior approval. However, we have provided courtesy copies of this statement to both the IRS and the Treasury Department in advance of this hearing.

³ See National Taxpayer Advocate 2010 Annual Report to Congress, vol. 2, § 2, 14 (Research Study: *The Patient Protection and Affordable Care Act: An Initial Analysis of the Implementation Challenges*).

⁴ See IRC § 7803(c).

By statute, TAS must make available at least one local taxpayer advocate (LTA) in each state. We recently have been assisting nearly 300,000 taxpayers a year with IRS disputes and account problems, including all taxpayer cases referred by congressional offices.⁵ Regarding systemic problems that affect groups of taxpayers, we work within the IRS to resolve problems to the extent possible, and I flag unresolved problems in my annual reports to Congress. We focus on tax administration concerns – not broader tax policy – and my position is nonpartisan.

Second: As a preface to the specific points that follow, I note that Congress in recent years has tasked the IRS with administering a number of social and economic benefit programs that require the IRS to go beyond its main historical role as the nation's tax collector. These programs include the disbursement of Economic Stimulus Payments, three different versions of the First-Time Homebuyer Credit, and the Making Work Pay credit – with precedents that can be traced back to enactment of the Earned Income Tax Credit (EITC) under President Ford in 1975.⁶ Because of the IRS's primary role as an enforcement agency, revenue officers, revenue agents, and other IRS employees are primarily trained in enforcement techniques rather than customer service, not to mention social work. This enforcement-oriented approach has created problems with EITC administration.⁷ To better enable the IRS to fulfill its dual roles of tax collector and benefits administrator, I have recommended in the past that the IRS revise its mission statement to reflect its two distinct roles.⁸ In my view, the IRS's new role in administering large portions of the ACA makes the need for a revised mission statement even more important.⁹

I. Since Publishing a 2010 Study on the Challenges Posed by the Law, the National Taxpayer Advocate Has Been Closely Monitoring IRS Implementation of the ACA.

In 2010, the National Taxpayer Advocate published a study analyzing administrative challenges posed by the four major ACA tax provisions – namely,

⁵ See National Taxpayer Advocate FY 2013 Objectives Report to Congress 68.

⁶ See IRC §§ 32, 36, 36A, 6428.

⁷ See National Taxpayer Advocate 2007 Annual Report to Congress, vol. 2 (Research Study: *The IRS EIC Audit Process – A Challenge for Taxpayers*); National Taxpayer Advocate 2004 Annual Report to Congress, vol. 2 (Research Study: *EITC Audit Reconsideration Study*); National Taxpayer Advocate 2003 Annual Report to Congress 26 (Most Serious Problem: *Earned Income Tax Credit Compliance Strategy*).

⁸ See National Taxpayer Advocate 2010 Annual Report to Congress 15 (Most Serious Problem: *The IRS Mission Statement Does Not Reflect the Agency's Increasing Responsibilities for Administering Social Benefits Programs*).

⁹ See National Taxpayer Advocate 2009 Annual Report to Congress, vol. 2, § 4, 75 (Research Study: *Running Social Programs Through the Tax System*).

the small business health-care tax credit, the premium assistance tax credit, the individual insurance requirement, and the employer requirement. (The first provision went into effect in 2011 while the latter three provisions become effective in 2014.)¹⁰ The 2010 report identified the ACA as a significant new piece of the historically growing portfolio of social provisions administered by the IRS.¹¹ In a recommendation consistent with my earlier suggestion that the IRS adopt a dual mission statement (as discussed above), the report recommended hiring social workers to answer ACA telephone calls. Furthermore, the report anticipated many of the accomplishments as well as ongoing concerns of ACA implementation. Since the 2010 report, my office has monitored ACA preparation closely.

Some of the concerns set forth in the 2010 report have been addressed through development of regulatory and computing infrastructure with related business mechanisms. For example, various regulations now define "household income" and set the parameters of privacy and information sharing.¹² As discussed below, the IRS has prepared a compliance mechanism for uninsured individuals. (In any case, the premium assistance tax credit may act as an incentive for eligible individuals to file tax returns.) These are significant accomplishments as far as they go.

In addition, the 2010 report anticipated several concerns. First, I believe the IRS needs to supplement its core ACA implementation team with inter-divisional staff including TAS, to make sure the full range of potential taxpayer concerns and problems is considered and addressed. Second, a top priority of this team should be communication and outreach to the many Americans who will now interact with the IRS on health insurance for the first time. In particular, these taxpayers may need education on the method by which the premium assistance tax credit is advanced to insurers and later reconciled with their tax returns. Finally, channels must be open for taxpayer referrals where another agency makes a determination that the IRS must execute, and *vice versa*. I remain confident the IRS can meet these challenges if it continues on its current course and receives adequate resources to meet its statutory duties.

II. The IRS Has Made Significant Progress Toward ACA Implementation.

Since ACA enactment, the IRS has been working through the major challenges, making significant progress. The IRS has published detailed rules and

¹⁰ See IRC §§ 36B, 45R, 4980H, 5000A.

¹¹ See also National Taxpayer Advocate 2011 Annual Report to Congress, vol. 2, § 1, 44 (Research Study: *From Tax Collector to Fiscal Automaton: Demographic History of Federal Income Tax Administration, 1913-2011*) (identifying historical advent of socio-economic provisions).

¹² See Treas. Reg. § 1.36B-1(e), 77 Fed. Reg. 30,377 (May 23, 2012); Prop. Treas. Reg. § 301.6103(l)(21)-1, 77 Fed. Reg. 25,378 (Apr. 30, 2012).

regulations, accelerated the development of information technology (IT), planned a procedure for secure information sharing, and prepared compliance mechanisms. The lead-time provided by the ACA has been very helpful for the IRS, and at this point, it appears the IRS has used the time well.

A. Timely Guidance

Since the 2010 enactment of the ACA, the IRS has produced a significant amount of guidance that will enable taxpayers to plan for ACA implementation. To date, the IRS has published 14 regulations (Treasury Decisions), eight proposed regulations, and seven revenue rulings and procedures.¹³ For example, some of this guidance clarifies the small business health-care tax credit, premium assistance tax credit, and information sharing process.¹⁴ I view the early publication of guidance as very taxpayer-friendly, reflecting the IRS's effort to offer advance guidance on a complex law, well before many provisions even take effect. Simply put, advance guidance enables taxpayers and businesses to plan.

B. Accelerated Development of Information Technology

On an accelerated calendar, the IRS is developing business requirements for computers and other IT, allowing for repeated advance testing of unique ACA systems. Advance testing should enable the IRS to identify and fix problems in time for implementation. After the IT systems are in place, the IRS will be able to shift resources from IT to customer service, where future needs will lie.

C. Planning of Secure Information Sharing

Combining regulatory and IT preparation with process planning, the IRS has outlined ACA information sharing. In general, taxpayers seeking health insurance and a premium assistance tax credit through an Exchange will supply names, Social Security numbers (SSNs), and income data for themselves and their dependents to the Exchange.¹⁵ An electronic model for this application process is the Free Application for Federal Student Aid (FAFSA), where an applicant may retrieve IRS data online for income verification by the Department of Education for college grants and loans.¹⁶ An Exchange will be able to verify data with the Department of Health and Human Services (HHS), which has

¹³ The legal guidance is posted at <http://www.irs.gov/newsroom/article/0,,id=222814,00.html> (last visited July 25, 2012).

¹⁴ See IRS Notice 2010-82, 2010-2 C.B. 857; Treas. Reg. §§ 1.36B-0 ff.; Prop. Treas. Reg. § 301.6103(l)(21)-1.

¹⁵ ACA § 1411(b), 124 Stat. 119, 224 (2010).

¹⁶ See IRS Data Retrieval Tool at <http://www.fafsa.ed.gov/> (last visited July 25, 2012).

authority under the ACA to obtain IRS data and then disclose any inconsistency to the Exchange.¹⁷

HHS or an Exchange may use IRS data only for ACA purposes, subject to rigorous statutory safeguards that require recordkeeping, secure storage, restricted access, reporting on safeguards, and shredding or otherwise destroying data after use.¹⁸ These safeguards already apply to state tax agencies across the country that routinely receive IRS data pursuant to existing law and implementing agreements.¹⁹ Under the ACA, implementation agreements negotiated among the IRS, HHS, and Exchanges will specify that the information is to be used solely for health insurance-related purposes and include safeguard requirements for information sharing. Through experience, planning, IT programming, and regulatory rulemaking, the IRS has prepared for secure information sharing.²⁰

D. Preparation of Compliance Mechanisms

Generally, the ACA requires uninsured individuals to obtain health coverage or pay a prescribed amount that the IRS may collect by offsetting a tax refund.²¹ Applicable individuals shall include this amount on their federal income tax return.²² At the same time, the IRS will receive information reports from every health insurance issuer, self-insured health plan, government-sponsored health insurance program, and other entity that provides minimum essential coverage identifying each insured individual.²³ By the process of elimination, the IRS should be able to identify uninsured individuals who do not show the prescribed amounts on their returns. Categorized as an "assessable penalty" under the tax

¹⁷ See IRC § 6103(l)(21).

¹⁸ See IRC § 6103(p)(4).

¹⁹ See IRC § 6103(d).

²⁰ Another privacy issue would be that under the ACA employer requirement, an applicable large employer may be liable for an assessable payment for failure to offer health coverage if an employee instead receives a premium assistance tax credit. See IRC § 4980H(a). Consequently, it is possible that a large employer may wish to ascertain the employee's eligibility for the credit. In this case, the large employer may obtain the employee's name and income threshold but not taxpayer return information. See ACA § 1411(f)(2)(B), 124 Stat. 119, 229 (2010).

²¹ See IRC § 5000A.

²² See IRC § 5000A(b).

²³ See IRC § 6055(a). Among other information, the "annual returns" shall report "the dates each individual was covered under minimum essential coverage during the calendar year." Notice 2012-32, 2012-20 I.R.B. 910.

law, this amount, capped by the average annual premium for qualifying private health insurance, is subject to refund offset.²⁴

About three-fourths of individual income tax returns claim refunds, averaging about \$3,000.²⁵ Consequently, it is likely that sufficient funds will be available for offset. Both offset and comparison of taxpayer returns with information reports are largely automated processes. While not dispositive, third-party information reports are a helpful indicator that will enable the IRS to operate a suitable compliance mechanism.²⁶

III. The Taxpayer Advocate Service Has Participated in ACA Preparation.

Even as the IRS has planned for the ACA, TAS has made its own preparations. Employees throughout TAS, most of whom serve taxpayers directly, have taken ACA training focused on issues most likely to come before Local Taxpayer Advocate (LTA) offices. With taxpayer service in mind, TAS has programmed an online tool to help small businesses estimate the amount of their health-care tax credit. To monitor overall IRS progress, TAS representatives have attended regular ACA briefings. TAS attorneys and other staff have reviewed and commented on drafts of ACA rules and regulations produced by the IRS. In conjunction with market research on taxpayer needs, TAS has collected data on health coverage. TAS plans more training before key provisions of the ACA take effect.

A. TAS Employees Have Taken ACA Training.

Since ACA enactment, TAS has developed written and video training materials on provisions likely to affect taxpayers who seek assistance from LTA offices. These materials present the four major ACA tax provisions, that is, the premium assistance tax credit, individual insurance requirement, and employer requirement, as well as the small business health-care tax credit, which received more in-depth discussion because of its early effective date, supplemented by an

²⁴ See IRC § 5000A(c), (g). For single individuals in 2016, the Congressional Budget Office has projected the relevant premium at \$4,500-\$5,000. See Cong. Res. Serv., *Individual Mandate & Related Info. Requirements Under ACA*, R41331 (July 2, 2012) 10.

²⁵ National Taxpayer Advocate FY 2012 Objectives Report to Congress 2. For CY 2010 and 2011, 77 and 75 percent of all individual returns claimed refunds averaging \$3,003 and \$2,913, respectively. IRS, *2011 and Prior Year, Filing Season Statistics, Cumulative Through the Weeks Ending 12/31/10 and 12/31/11* (Jan. 9, 2012), <http://www.irs.gov/newsroom/article/0,,id=252176,00.html>. Taxpayers who filed on or before Feb. 26, 2010, and Feb. 25, 2011, claimed refunds at an even higher rate – 85 and 87 percent, averaging even higher – \$3,149 and \$3,129, respectively. IRS, *2011 and Prior Year Filing Season Statistics, Cumulative Through the Weeks Ending 2/26/10 and 2/25/11* (Jan. 9, 2012), <http://www.irs.gov/newsroom/article/0,,id=237562,00.html>.

²⁶ See *Portillo v. Comm'r*, 932 F.2d 1128, 1134 (5th Cir. 1991) (holding that the IRS “had some duty to investigate” the accuracy of an information return), *rev’d in part* T.C. Memo. 1990-68.

overview of other ACA tax provisions.²⁷ Employees throughout TAS have been required to review these training materials over the past couple of years.

The training prepares TAS employees to contribute to ACA operations in three ways: (1) outreach and education; (2) resolution of taxpayer problems; and (3) ongoing systemic advocacy. As the 2014 implementation date nears, TAS will train employees on case-specific guidance. As part of a communications strategy discussed below, LTAs will share with taxpayers and stakeholder groups information about how to avoid problems. Finally, upon ACA implementation, TAS will resolve taxpayer cases, identify systemic problems, and advocate for improvements. These activities are consistent with the approach TAS takes to any major legislative change.

B. TAS Has Programmed a Small Business Health-Care Tax Credit Estimator.

The ACA contains an incentive for small businesses to offer health insurance in the form of a tax credit proportionate to premiums paid.²⁸ As is always the case with tax credits, the amount is realized upon filing the return after the close of the taxable year. Consequently, the incentive effect may be limited if the business cannot predict the amount. With customer service in mind, a TAS employee programmed an online tool to estimate the credit based on input about the business, insurance plan, and employees. The Estimator is intended to be educational, leading the business to complete the requisite IRS form or consult a tax professional to obtain the actual credit.²⁹ Before posting on the Web, the Estimator is in the final stages of review by ACA experts from the IRS core implementation team working closely with TAS staff, in an excellent example of collaboration between the IRS and TAS.

C. TAS Employees Have Attended Briefings and Reviewed Rulemakings.

As the IRS has been designing the IT and regulatory infrastructure for ACA implementation, TAS officials and employees have attended regular briefings to maintain a current view of activity and offer insight from the perspective of taxpayer rights and taxpayer needs. In addition, TAS attorneys and other staff have reviewed and commented on drafts of the rules and regulations described above. These contributions are consistent with the oversight and advocacy role of TAS within the IRS.

²⁷ See National Taxpayer Advocate FY 2012 Objectives Report to Congress 21; National Taxpayer Advocate 2010 Annual Report to Congress, vol. 2, § 2, 21 (Research Study: *The Patient Protection and Affordable Care Act: An Initial Analysis of the Implementation Challenges*); ACA § 1421(f) (containing 2011 effective date for small business credit).

²⁸ See IRC § 45R.

²⁹ See Form 8941, *Credit for Small Employer Health Insurance Premiums*.

D. TAS Has Surveyed Taxpayer Needs.

To identify and understand the underserved taxpayer population, TAS developed a survey in consultation with a market research firm, which administered the survey earlier this year. Among demographic and other characteristics of the population, the survey inquired whether respondents have health coverage and, if so, where they obtained it. For business owners, the survey asked whether they are offering health coverage to their employees. The answers will come in the context of attributes such as age, income, family size, use of tax return preparers, attitudes about the IRS, awareness of TAS services, and Internet usage. Analysis of the results will continue until the end of the year.

Additionally, TAS is consulting with the research firm on a survey targeting Spanish-speaking U.S. residents not polled by the earlier survey. As with the survey described above, this survey will contain questions about health coverage in the context of demographic and other characteristics. This companion survey will extend our knowledge of underserved taxpayers to this important segment of the population. Survey administration and data development will be completed next year. Results from both surveys will enable TAS to prepare a communications and outreach strategy based on the health-care and tax needs of the underserved population.

IV. Significant Concerns Remain with Respect to ACA Implementation.

While TAS and the IRS as a whole have prepared extensively, I remain concerned that the upcoming months of ACA implementation will require even more intensive activity. Starting immediately, the IRS should include TAS representatives on ACA teams. Likewise, the IRS and sister agencies now need to formulate a communications strategy in anticipation of public questions. In particular, taxpayers require education about the need to update information relating to eligibility for the premium assistance tax credit. Similarly, the IRS, Exchanges, and other agencies that share responsibility for the administration of ACA provisions need to open channels for inter-agency referral of customer issues. Among these issues may be identity (ID) theft, which continues to plague the tax system, where it will have ramifications for ACA income verification. Additionally, small businesses need guidance on complex provisions targeted at them. And as always, the IRS needs adequate resources to administer the tax code Congress has written. With the requisite actions and resources, I believe the IRS can address the potential sticking points associated with ACA implementation.

A. The IRS Should Include TAS Staff on Implementation Teams.

As discussed above, Congress created the position of the National Taxpayer Advocate and the Office of the Taxpayer Advocate to serve as the "voice of the

taxpayer" within the IRS.³⁰ Based on congressional hearings and other input, members of the tax-writing committees were concerned that because IRS employees often possess an enforcement mentality, the National Taxpayer Advocate was needed to ensure that IRS planning and policy give adequate weight to protecting taxpayer rights and minimizing taxpayer burden. Within the IRS, TAS representatives participate as full members on many cross-functional teams, but the IRS to date has declined to include TAS representatives on ACA implementation teams, preferring to provide us with periodic updates. This approach made sense in the initial planning stages. However, as the final stages of ACA implementation approach, the IRS must give greater priority to clear and effective communication with taxpayers, businesses, and the Exchanges, and it must ensure that taxpayers who actually or seemingly run afoul of ACA requirements or IRS filters are treated fairly and in a prompt manner. TAS's job is to identify potential glitches and recommend solutions, and I am concerned that if the IRS excludes the "voice of the taxpayer" from full participation in the implementation of the ACA, the risk of taxpayer and employer harm will be needlessly high.

B. Planning of Public Communication Is Too Slow.

The National Taxpayer Advocate is disappointed that IRS and inter-agency planning of an ACA public communications strategy is proceeding slowly as deadlines approach. By March 1, 2013, all employers across the country must notify their employees of a right to purchase health insurance – with a potential government subsidy – at an Exchange, in turn scheduled to open October 1, 2013.³¹ Even though this notice is not a tax requirement, it may prompt taxpayers to flood IRS call centers with inquiries because the subsidy takes the form of a tax credit. None of the responsible agencies should wait in planning how to help taxpayers, who will be bombarded by information, to make sense of the new provisions. Moreover, the tax profession has decades of relevant experience in communicating with a low income population in the case of the EITC.³² In short, the IRS, including TAS, should join now with other responsible agencies, as well as community organizations that have relevant experience, to develop and deploy a targeted communications strategy.³³

³⁰ See Rep't of the Comm. on Restructuring the IRS: *A Vision for a New IRS* 48 (June 25, 1997).

³¹ See Fair Labor Standards Act of 1938, § 18B, as added by ACA § 1512, 124 Stat. 119, 252 (2010). See also 45 C.F.R. § 155.410, 77 Fed. Reg. 18,462 (Mar. 27, 2012).

³² See Written Statement of Nina E. Olson, National Taxpayer Advocate, *Hearing on Improper Payments in the Administration of Refundable Tax Credits*, Before the Subcomm. on Oversight, Comm. on Ways & Means, U.S. House of Reps. (May 25, 2011) 8 (describing IRS partnerships with organizations that serve the low income community to educate taxpayers about the EITC).

³³ Furthermore, the EITC model raises the issue of institutional processes in administering a subsidy through the tax system. In the case of the EITC, the use of a tax credit eliminates a traditional welfare application process. By contrast, the ACA introduces an Exchange application process for the premium assistance tax credit. These contrasting designs warrant further study

C. Taxpayers Require Education on the Need to Update Information.

Certain ACA provisions have tax consequences that require taxpayers to understand their role goes beyond traditional return-filing at year-end. In particular, taxpayers at certain income levels may qualify for a premium assistance tax credit advanced by the government to their insurer.³⁴ If their income at year-end turns out to be more than anticipated, the credit may be less than the amount advanced, and the IRS may recover the excess as a tax, below a ceiling for low income taxpayers.³⁵ To avoid receiving an excess, taxpayers may need to update information if their income or other relevant circumstances change.³⁶ Because an application may base income on the last tax return (*i.e.*, the one filed in the current year relating to the year that just ended), a couple of years' worth of life changes could transpire by the time of reconciliation between the advance and ultimate credit amounts. In effect, the premium assistance tax credit requires not only an initial application and a year-end tax return but ongoing updates on major life changes throughout the year. Because this updating role will be new, education of taxpayers is necessary to avoid unexpected tax consequences. The importance and manner of providing updates should be part of the communications strategy discussed above.

D. The ACA Will Require a Significant Level of Inter-Agency Referrals.

For the premium assistance tax credit and individual insurance requirements, the IRS shares responsibility for taxpayer service with HHS and the Exchanges, requiring inter-agency coordination and mutual referral of customers. For an application, the taxpayer may retrieve IRS data for income verification at the Exchange. If the data are inaccurate, the taxpayer may present updated documentation or other rectifying evidence to the IRS, as may be the case in a routine tax audit. It is unclear whether the Exchange would adhere to the same evidentiary standards.³⁷ Consider the following illustration.

regarding implications for tax simplification and overall burden reduction. *See generally* National Taxpayer Advocate 2010 Annual Report to Congress, vol. 2, § 6, 116 (Research Study: *Evaluate the Administration of Tax Expenditures*) (distinguishing between mechanical and discretionary tax subsidies).

³⁴ See IRC § 36B.

³⁵ See IRC § 36B(f). "[S]ection 36B(f)(2)(B) places a graduated set of caps on the additional tax liability for taxpayers with household income under 400 percent of the FPL [Federal Poverty Level]. The repayment limitation amounts range from \$600 to \$2,500 (one-half that amount for single taxpayers) depending on FPL, and are adjusted to reflect changes in the cost of living beginning in 2015." 76 *Fed. Reg.* 50,933-934 (Aug. 17, 2011).

³⁶ See 45 C.F.R. § 155.330 (Eligibility redetermination during a benefit year), 77 *Fed. Reg.* 18,458 (Mar. 27, 2012).

³⁷ HHS has stated that "we intend to propose the details of the individual eligibility appeals processes, including standards for the Federal appeals process, in future rulemaking." 77 *Fed. Reg.* 18,384 (Mar. 27, 2012).

Example: A taxpayer inadvertently enters an erroneous Taxpayer Identification Number (TIN) for a dependent on a tax return. After filing, the IRS reduces the taxpayer's refund, sending a "summary assessment" notice denying tax benefits with respect to the dependent. In response, the taxpayer forwards the correct TIN to the IRS, which then restores the benefits. This process can take several months.³⁸

Now that health coverage as well as tax consequences may flow from a correction like this one, the IRS has an even greater incentive to improve issue-resolution processes. It may very well be that effective implementation of ACA provisions will improve certain aspects of traditional tax administration.

As discussed above, the IRS ultimately will adjust a credit amount based on year-end income, which may have changed since the taxpayer applied to the Exchange. To avoid unexpected tax consequences, the IRS may need to alert taxpayers of the ongoing need to update their information at the Exchange.

An uninsured individual may be subject to collection of a prescribed amount by the IRS except, *inter alia*, in case of hardship.³⁹ In pertinent part, the ACA defines a hardship as incapability of obtaining coverage as determined by HHS upon application by the individual.⁴⁰ In attempting to collect from an individual who complains of hardship, the IRS may need to make a referral to HHS.

In other words, taxpayers may ricochet between the IRS, HHS, and Exchanges. To answer resulting calls, telephone representatives of the IRS, including TAS, will have to: (1) listen to the taxpayer long enough to identify the agency responsible for the problem and (2) maintain a complete "rolodex" of contacts to make the right referral. In short, inter-agency coordination is essential, especially for individuals in vulnerable circumstances. Because of TAS's role and experience with such individuals, the IRS can better address this concern by including representatives of the National Taxpayer Advocate as members of the inter-agency teams, as recommended above.

E. Identity Theft Poses a Serious Concern.

As the National Taxpayer Advocate previously has stated, ID theft continues to plague taxpayers, with more than half a million cases in the IRS, and will have

³⁸ See National Taxpayer Advocate 2011 Annual Report to Congress, vol. 2, § 4, 113, 138 (Research Study: *Math Errors Committed on Individual Tax Returns: A Review of Math Errors Issued for Claimed Dependents*).

³⁹ See IRC § 5000A(e). Other exceptions include those taxpayers with incomes below the filing threshold.

⁴⁰ See IRC § 5000A(e)(5).

ramifications for the ACA.⁴¹ In general, tax-related identity theft occurs when a thief intentionally uses another individual's SSN on a false tax return claiming an unauthorized refund.⁴² If the IRS screens out that return due to suspected fraud, the IRS will freeze the account under the victim's SSN pending resolution, in a potentially lengthy process.⁴³ Meanwhile, if the victim attempts to retrieve IRS data for an Exchange application, his or her account will be frozen. The Exchange may need to refer the victim to the IRS to resolve the ID theft while supplying instructions on alternative ways to prove income level, *i.e.* an inter-agency referral as discussed above.

F. Small Businesses Need Further Guidance.

As previously noted, the ACA contains an incentive for small businesses to offer health insurance in the form of a tax credit proportionate to premiums paid.⁴⁴ Yet a decision to offer health insurance entails technical questions. For example, must the insurance plan comply with an ACA prohibition on discriminating in favor of highly-compensated individuals?⁴⁵ Questions like these relate back to the IRS's rulemaking efforts as well as the overall public communication strategy.

G. The IRS Needs Adequate Resources.

The National Taxpayer Advocate does not take a position on policy issues, and therefore offers no opinion about the wisdom of the ACA. With or without the ACA, however, it is essential for the taxpaying public that the IRS be adequately funded to administer whatever Congress directs it by statute to do. The National Taxpayer Advocate's 2011 Annual Report to Congress identified the combination of the expanding IRS workload and its shrinking resources as the most serious

⁴¹ Through the end of June 2012, there were 504,019 open identity theft cases across multiple operating divisions.

⁴² See Written Statement of Nina E. Olson, National Taxpayer Advocate, *Hearing on Identity Theft and Income Tax Preparation Fraud*, Before the Subcomm. on Crime, Terrorism & Homeland Security, Comm. on the Judiciary, U.S. House of Reps. (June 28, 2012) 5 (describing tax refund-related ID theft); see also IRM 10.5.3.2, *Identity Protection Program Servicewide Identity Theft Guidance* (July 9, 2012).

⁴³ See National Taxpayer Advocate 2011 Annual Report to Congress 58 (Most Serious Problem: *Tax-Related Identity Theft Continues to Impose Significant Burdens on Taxpayers and the IRS*).

⁴⁴ See IRC § 45R.

⁴⁵ See Notice 2011-1, 2011-2 I.R.B. 259 (affording transition relief from compliance with prohibition on discrimination pending publication of regulatory guidance). Additional questions would be the applicability of a pre-existing IRC § 4980D(d) exception for small business, and the scope of the requirement for a statement of a grandfathered plan exempt from major ACA provisions. See Treas. Reg. § 54.9815-1251T(a)(2)(i), 75 *Fed. Reg.* 34,538 (June 17, 2010) ("To maintain status as a grandfathered health plan, a plan or health insurance coverage must include a statement, in any plan materials provided to a participant or beneficiary describing the benefits provided under the plan or health insurance coverage, that the plan or coverage believes it is a grandfathered health plan within the meaning of section 1251 of the Patient Protection and Affordable Care Act and must provide contact information for questions and complaints.")

problem facing U.S. taxpayers.⁴⁶ Because of this imbalance between responsibilities and resources, the IRS is now unable to answer roughly one-third of the tens of millions of calls it receives from taxpayers each year, or to process timely about half the correspondence it receives from taxpayers in response to tax adjustment notices.⁴⁷ Similarly, the IRS cannot detect and address noncompliance as well as it should. Furthermore, the IRS is now unable to maximize the collection of revenue due under the tax laws enacted by Congress, thus contributing to the budget deficit – despite the fact that the IRS brings in \$200 in revenue for every dollar it receives in appropriated funds and despite widespread acknowledgement that the IRS would bring in substantially more than \$1 for each additional dollar it receives.⁴⁸ I am particularly concerned that taxpayer service suffers the most when IRS funding is inadequate, and I therefore encourage the Committee to ensure that U.S. individuals and businesses trying to pay their taxes are not shortchanged.

V. Conclusion

The National Taxpayer Advocate continues to monitor ACA implementation by the IRS. In general, I believe the IRS has done a good job of preparing, but some challenges remain. In particular, the IRS has made significant progress on rulemaking, IT, and related business mechanisms. At the same time, TAS has trained employees and otherwise participated in ACA preparation. Now the IRS should join with TAS, other responsible agencies, and stakeholder organizations to take on the final challenges of ACA implementation, remaining vigilant to unanticipated problems.

⁴⁶ National Taxpayer Advocate 2011 Annual Report to Congress 3 (Most Serious Problem: *The IRS Is Not Adequately Funded to Serve Taxpayers and Collect Taxes*).

⁴⁷ IRS Jt. Operations Ctr., *Snapshot Reports: Enterprise Snapshot* (FY 2012, through July 14, 2012); IRS Jt. Operations Ctr., *Weekly Enterprise Adjustments Inventory Rep't* (week ending July 21, 2012).

⁴⁸ In FY 2011, IRS collected about \$2.42 trillion on a budget of about \$12.1 billion. See Dep't of the Treas., *FY 2013 Budget in Brief* (showing FY 2011 enacted levels); Gov't Accountability Office, *Financial Audit: IRS's Fiscal Years 2011 and 2010 Financial Statements*, GAO-12-165 (Nov. 2011) 63 (showing FY 2011 tax revenue).

Chairman ISSA. I thank the gentlelady.

I now ask unanimous consent the 2010 annual report to Congress be placed in the record.

Without objection, so ordered.

Chairman ISSA. The gentlelady mentioned a 2011 report. Do you have a copy of that with you?

Ms. OLSON. I do not, but I can certainly get it to you for the record.

Chairman ISSA. Then I would ask unanimous consent that also be placed in the record.

Without objection, so ordered.

Professor Jost, thank you very much. You are recognized.

STATEMENT OF TIMOTHY JOST

Mr. JOST. Thank you. Thank you, Chairman Issa, Ranking Member Cummings, Committee members, for this opportunity to address you today on the role of the Internal Revenue Service in health care reform. My remarks today specifically address Mr. Cannon's assertions which he will be making shortly that the IRS rule that permits Federal exchanges to issue tax credits is illegal.

If Mr. Cannon is right, many constituents of Committee members will lose tax relief that could give them access to affordable health insurance. Just for 2014, 1.9 million Floridians would lose \$7.7 billion in Federal tax relief, 593,000 Indianans would lose \$2.2 billion, over 1 million Ohioans would lose \$4 billion, 2.6 million Texans would lose over \$10 billion in Federal tax relief to help make health insurance affordable.

Fortunately, Mr. Cannon's position is based on a misunderstanding of the law, its structure, and history. The exchange is fundamentally a market for health insurance, but exchanges will also ensure that health insurance consumers get value for money and access to premium tax credits.

Section 1311 of the Affordable Care Act asks the States to establish exchanges, but Section 1321 authorizes HHS to establish a Federal exchange in States that choose not to, which is likely to include many States of members of this Committee.

Mr. Cannon believed that Federal exchanges cannot issue premium tax credits. This assertion was made earlier in this hearing. Because two subsection of Section 36(b) of the Internal Revenue Code, which establishes eligibility for tax credits, refer to "persons enrolled through an exchange established by the State under Section 1311," Mr. Cannon argues that this means only State and not Federal exchanges can offer tax credits.

The Affordable Care Act as amended by the Health Care and Education Reconciliation Act, however, explicitly provides that Federal exchanges can issue tax credits.

When I teach first-year law students how to read a statute, I tell them you start with the definition section. Section 1563.C of the Affordable Care Act defines exchanges to mean "an American health benefits exchange established under Section 1311." Section 1311 literally states that a State shall establish an exchange, and section 1311.D describes and exchange as an exchange established by a State.

Because Congress cannot, however, Constitutionally require a State to establish exchanges, Section 1321.C provides that the HHS Secretary shall establish and operate such exchange within a State, referring to the 1311 State, if a State fails to do so.

Under the Affordable Care Act definition of exchange, a Section 1321 exchange becomes a Section 1311 exchange established by the State. This is reinforced by Section 1321, itself, which, again, refers to such exchange, referring to the earlier required 1311 required State exchange. Under ACA, therefore, all exchanges, Federal and State, are 1311 exchanges established by the State by definition.

Other sections of the ACA direct all exchanges, Federal and State, to manage Federal tax credit functions, including Section 1413, which requires all exchanges to use streamlined applications and eligibility assessments to qualify persons for premium tax credits.

Most importantly, a third subsection of Section 36(b), itself, clarifies premium tax credits are available through both State and Federal exchanges.

This subsection was added to the ACA by the Reconciliation Act, which, as a later adopted statute, takes precedence over the original ACA if there were any contradiction.

Mr. Cannon's interpretation is also refuted by the legislative history of the ACA as demonstrated in my extended remarks, which refer to repeated references to all States having premium tax credits available.

Mr. Cannon claims to have found a statement by Senator Baucus acknowledging that only State exchanges could issue premium tax credits. I would be happy to introduce that colloquy between Senator Baucus and Senator Ensign into the record. It cannot be read to say that.

Perhaps most importantly, the CBO and JCT have consistently assumed the availability of premium tax credits through State and Federal exchanges since 2009, and, indeed, the CBO's report from two weeks ago at footnote 14 explicitly recognizes that both Federal and State exchanges will issue premium tax credit.

Finally, Section 36(b) of the IRC expressly grants the IRS authority to write regulations if there were any ambiguity in the statute. Under the Chevron Doctrine, the IRS's interpretation of the statute would be accepted by the courts, as a recent Congressional Research Service legal analysis affirms.

In sum, premium tax credits will be available to middle income uninsured citizens of all of your States, not just Chairman Issa's and Mr. Cummings' States, which are going to have State exchanges.

Thank you.

[Prepared statement of Mr. Jost follows:]

**House Committee on Oversight and Government Reform
The Role of the Internal Revenue Service in Health Reform
Testimony of Timothy Stoltzfus Jost**

Thank you Chair Issa, Ranking Member Cummings, and Committee Members for the opportunity to address you today on the important topic of the role of the Internal Revenue Service in the reform of our health care system. My name is Timothy Stoltzfus Jost and I am a law professor at Washington and Lee University. I am also a consumer representative to the National Association of Insurance Commissioners and an elected member of the Institute of Medicine.

My remarks today address Mr. Cannon's assertions that the Department of the Treasury's rule providing for the federal exchange to issue tax credits to middle-income Americans that will make it possible for them to afford health insurance is not authorized by the Affordable Care Act. Many of the uninsured middle-income Americans who will benefit from these tax credits are constituents of members of this committee. I assume, therefore, that this is a matter of great concern to you. Fortunately, Mr. Cannon's position is based on a misunderstanding of the law, its structure, and history, as I will explain.

The Affordable Care Act Exchanges and Premium Tax Credits

To understand this issue it is necessary to understand the role of the exchange in the Affordable Care Act. The American Health Benefits Exchange is fundamentally a market in which health insurance is bought and sold. The exchange is also responsible for ensuring that insurers who sell their products through the exchange meet certain minimum standards to ensure that individuals and small employers who purchase in the exchange are getting value for their dollar. Finally, the exchange is the gateway to federal premium tax credits, Medicaid, and other assistance programs for those unable to afford health insurance. The exchange concept has until very recently enjoyed broad bipartisan support as a tool for making private sector health insurance widely available and affordable to Americans.

Section 1311 of the Affordable Care Act asks the states to establish American Health Benefits Exchanges. As we all know, however, the federal government cannot order a state to operate a federal regulatory program, so section 1321 of the ACA authorizes the Secretary of Health and Human Services to establish a federally facilitated exchange in states that choose not to establish their own exchange.

Mr. Cannon takes the position that federal exchanges cannot offer premium tax credits. He bases this opinion on two subsections of section 36B of the Internal Revenue Code (created by section 1401 of the ACA), which provides for tax credits to help middle-income Americans afford health insurance. In defining the premium tax credit amount and the coverage months for which it is available, sections 36B(b)(2) and 36B(c)(2)(A) refer to persons "enrolled in [a qualified health plan] through an Exchange established by the State under section 1311." Mr. Cannon argues that this language precludes premium

tax credits being issued through the exchanges operated in the states by the federal government. If this is true, it is likely that many—perhaps most--Americans will be denied access to an important middle-class tax benefit in 2014, as it now appears that many states will, at least initially, have federally facilitated exchanges.

In his recent article, Mr. Cannon, together with Professor Jonathan Adler of Case Western University, claims that this language is not only unambiguous but also intentional, that Congress intended to punish states that refused to establish exchanges by refusing premium tax credits to their residents.¹ Cannon and Adler further claim that final rules promulgated by the IRS making premium tax credits available through federal as well as state exchanges are unauthorized by law, and thus illegal.

If this claim is true, uninsured constituents of members of this committee stand to lose billions of dollars in federal tax relief that would have assisted them in purchasing health insurance. 1.9 million Floridians would lose \$7.7 billion in federal tax relief just in 2014; 593,000 Hoosiers would lose \$2.2 billion; over 1 million Buckeyes would lose over \$4 billion in tax credits; 382,000 Oklahomans would lose \$1.5 billion; and 2.6 million Texans would lose over \$10 billion dollars in federal tax assistance.² And this is just for 2014.

The Affordable Care Act Explicitly Authorizes Federal Exchanges to Provide Premium Tax Credits

Fortunately for your constituents, Mr. Cannon's claims are simply not true. If the sections that he cites were the only relevant sections of the Affordable Care Act, and if the legislative history and structure of the ACA could be simply ignored, his statutory construction claim would be plausible. But the availability of tax credits through federally facilitated exchanges is recognized through the language of the ACA, as amended by the Health Care and Education Reconciliation Act. The legislative history of the ACA also establishes that Congress understood that premium tax credits would be available through both federal and state exchanges. The IRS is explicitly authorized by Congress to interpret the statute and its interpretation of the law will be given deference by the courts. The existence of exchanges in every state was assumed both by the Congressional Budget Office and by both proponents and opponents of the ACA as it was being debated. Finally, the structure and purpose of the ACA requires that state or federal exchanges offer premium tax credits in every state.

I begin with the language of the ACA itself. The term "exchange" is a defined term under the ACA, a point that Mr. Cannon does not mention in his article but that would surely be paid great attention by the courts. Section 1563(b) of the ACA states: "The term 'Exchange' means an American Health Benefit Exchange established under section 1311 of the Patient Protection and Affordable Care Act." Section 1311 literally requires that the states "shall" establish an American Health Benefits Exchange by January 1, 2014. Because the Constitution prohibits the federal government from literally requiring states to establish exchanges, however, section 1321(c), provides that "the [HHS] Secretary shall (directly or through agreement with a not-for-profit entity) establish and

operate *such* Exchange within the State.” Under the ACA’s definition of exchange, the term “Exchange” in section 1321 exchange means a section 1311 exchange. This is reinforced by section 1321 itself, in which the term “such Exchange,” refers to the “required exchange” mentioned in section 1321(c)(1)(B)(i), which is to say the 1311 exchange. When section 1321 directs HHS to establish an “Exchange,” therefore, it means to establish a section 1311 exchange, which section 36B authorizes to provide premium tax credits.

Section 36B is not the only section of the ACA that imposes duties on the state and federal exchanges relevant to premium tax credits. Section 1311(d)(4)(G) requires exchanges to provide their enrollees premium calculators that include a deduction for premium tax credits. Section 1311(d)(4)(I), requires exchanges to forward to the IRS information about enrollees who are eligible for premium subsidies. Section 1311(d)(4)(J), requires an exchange to notify employers if their employees are receiving premium tax credits. Finally, section 1413 requires state and federal exchanges to use streamlined applications and eligibility assessments to help people qualify for “health subsidy programs,” which programs specifically include premium tax credits, see section 1413(e)(1). All of these sections apply to federal as well as state exchanges.

Most importantly, a third subsection of section 36B itself clarifies that premium tax credits are available through both state and federal exchanges. As you remember, the ACA is composed of the Senate version of the Patient Protection and Affordable Care Act, Public Law 111-148, and the Health Care and Education Reconciliation Act, Public Law 111-152. The Senate adopted the bill that became Public Law 111-148 in December of 2009, but the House adopted it only in March of 2010. Shortly thereafter, the House and Senate adopted the Reconciliation Act, through which the House made certain changes in the Senate bill. As a later-adopted statute, HCERA takes precedence over that of the PPACA, if there is a contradiction. Moreover, since the adoption of HCERA was necessary to secure House adoption of the Senate bill, it is doubly important that the provisions of HCERA be taken seriously. The House bill contained only a federal exchange. Section 1004 of HCERA adds to IRC section 36B, subsection 36B(f)(3) which requires both 1311 and 1321 exchanges to provide certain information regarding premium tax credits to the IRS and to taxpayers. Cannon and Adler admit the existence of this provision but simply say it is meaningless, as 1321 exchanges cannot authorize premium tax credits. This position, however, violates another canon of statutory construction—that every provision of a congressional enactment should be given effect.

It should be noted that several other sections of the ACA use the language on which Mr. Cannon relies--“an Exchange established by the State under section 1311.” One of them is section 2001 which prohibits states from reducing Medicaid eligibility until an exchange “Established by the State under section 1311” is operational.” If Mr. Cannon’s interpretation of the ACA is correct, states that decide not to establish a state exchange will be barred indefinitely from changing their Medicaid eligibility requirements. But this is not what the law means.

The Affordable Care Act's Legislative History also establishes that Federal Exchanges can offer Premium Tax Credits

Mr. Cannon's interpretation of the ACA is also refuted by the legislative history of the ACA. The Senate bill which became the ACA was derived from the S 1679,³ the Senate Health, Education, Labor and Pensions Committee bill and S 1796⁴ which emerged later from the Senate Finance Committee. Each of these bills included state and federal exchanges, which were called Gateways in the HELP bill.

The HELP bill (section 142, adding section 3104 of the Public Health Services Act) created an elaborate structure under which states could either establish exchanges themselves ("establishing states"), request the federal government to establish an exchange in the states ("participating states"), or fail to do either, in which case four years after the enactment of the statute the federal government would create a fallback exchange in the state. Premium tax credits were available in establishing and participating states, but would only be available through the federal fallback exchanges in states that complied with the employer responsibility provisions for state and local employees. In other words, the states were threatened with loss of premium tax credits, not for failing to establish exchanges but for not complying with the employer responsibility provisions for their employees.

The Finance Committee bill did not use this elaborate structure. In fact, the rules it creates are very similar to the final ACA. It creates section 2235 of the Social Security Act, which provides that states "shall" establish an exchange, and sets out the duties of the exchange. Section 2225(b) provides, in language very similar to current ACA section 1321, that HHS shall contract with a nongovernmental entity to operate an exchange in states that fail to "establish and operate" an exchange in states that fail to create one within 24 months. The Finance Committee Report⁵ refers to these federally established exchanges as "state exchanges." In a number of places, including the precursor of the current premium tax credit provision, the bill refers to exchanges "established by the state," but nowhere does it provide, as did the HELP bill, that premium tax credits would not be available in the any of the exchanges created by the federal government.

The provisions of the current ACA addressing this issue are taken largely from the Finance Committee bill, which makes sense because the Finance Committee has jurisdiction over tax matters. The punitive provisions of the HELP bill were abandoned.

The Senate debated the ACA extensively during November and December 2009. The version of the Act they were considering included both state and federal Exchanges. Throughout the debate, Senators assumed that tax credits would be available in all 50 states. Thus Senator Bingaman stated on December 4, 2009, that the ACA "includes creation of a new health insurance exchange in each State which will provide Americans a centralized source of meaningful private insurance as well as refundable premium tax credits to ensure that coverage is affordable."⁶ Senator Johnson stated on December 17, "the legislation will also form health insurance exchanges in every State," which will

“provide tax credits to significantly reduce the cost of purchasing that [insurance] coverage.”⁷

If Congress had meant to limit premium subsidies to state-established exchanges, as an incentive to States, one would have expected the Finance Committee report on S. 1796 to have mentioned this, and for at least one Senator to have pointed this out during the debate in November and December 2009.

Most importantly, the Congressional Budget Office (together with the Joint Committee on Taxation) provided Congress on November 30, 2009, with an analysis of the impact of the legislation on premiums that assumed that premium tax credits would be available in all states, making no distinction between federal and state exchanges.⁸ Over the next few days this analysis was discussed by Republican Senators Grassley,⁹ Enzi,¹⁰ and Coburn.¹¹ None raised what Cannon and Adler see as an obvious point—that the CBO analysis was flawed because it failed to recognize that premium tax credits would not be available though federally facilitated (sec. 1321) exchanges. In fact, the CBO repeatedly provided cost estimates of the ACA and HCERA in late 2009 and early 2010, but never suggested that premium tax credits might be reduced if states failed to establish exchanges. In its most recent report from two weeks ago updating ACA coverage estimates in the wake of the Supreme Court decision, the CBO and JCT reiterates again that premium tax credits will be available though state, federal, and partnership exchanges.¹² As Yale Professor Abbe Gluck notes in a recent blogpost¹³ (and forthcoming article), Senators often don’t listen to each other, but they all listen to the CBO, which assumed that premium tax credits would be available to all Americans in all states.

Mr. Cannon claims, however, to have found a smoking gun, a colloquy between Senators Baucus and Ensign during the Finance Committee debate on the bill, in which, they claim, Senator Baucus admits that premium tax credits could not be made available through federal exchanges. In fact, the colloquy, which Cannon and Adler edit beyond recognition, had nothing to do with federally facilitated exchanges, but rather with whether the Finance Committee or the Judiciary Committee had jurisdiction over malpractice reform legislation that Ensign wanted to attach to the bill. In fact, there is nothing in the legislative history of the ACA that supports the notion that premium tax credits will not be available through federal exchanges.

Mr. Cannon argues that Congress prohibited the federal exchanges from offering premium tax credits as a way of encouraging the states to adopt exchanges. It is in fact clear that Congress favored state exchanges, and offered generous grants to the states (which to date have totaled nearly \$850 million dollars with more on the way.¹⁴ States that fail to establish exchanges will also lose some control of their insurance markets. But Congress did not try to “coerce” states to create state exchanges by threatening their citizens with loss of billions of dollars of premium tax credits. Indeed, under the Supreme Court’s recent Medicaid decision, such coercion might have been suspect.

The Structure of the Affordable Care Act Makes it Clear that Federal Exchanges may offer Premium Tax Credits

Moreover, not only do a number of provisions of the ACA, already described, refer explicitly to federal and state exchanges performing functions relating to premium tax credits, but the entire structure of the ACA's insurance reforms are based on the availability of premium tax credits in all states. The ACA's guaranteed issue and community rating requirements apply to insurers in all states, regardless of whether they have federal or state exchanges. So do the ACA's risk mitigation programs. So does the ACA's individual mandate. The premium tax credits are intended to bring millions of new participants into insurance markets, and if they are not available in many states, the nature of insurance markets will change dramatically, increasing the risk of insurers and decreasing availability to middle-income Americans. If this was the intent of Congress, it surely would have made it far more evident.

The ACA is admittedly not a model of clear drafting. It was drafted by the Senate and not the House. It contains three sections with the same number (1563) and amends an existing provision of the Public Health Services Act inconsistently twice within the scope of a few pages. The Senate bill was not supposed to be the final law. Only Senate the election in Massachusetts in early 2010 made a conference committee bill that would have reconciled the House and Senate versions and cleaned up the current bill impossible. The courts are unlikely to find the "established by the state" language a "scrivener's error." But the courts will interpret the ambiguous language in the context of the ACA's structure and purpose, in light of the ACA's legislative history, and putting great weight on the HCERA amendment, and find that federally facilitated exchanges can in fact issue premium tax credits.

The Department of the Treasury is Authorized to Interpret Section 36B and the Courts will Defer to its Interpretation

Finally, the courts are likely to grant great deference to the IRS premium tax credit regulation. Section 36B explicitly grants authority to the IRS to interpret the section. A recent CRS Legal Analysis of this issue states clearly that under the ruling "Chevron doctrine," derived from the case of *Chevron v. NRDC*,¹⁵ courts will defer to the interpretation of the IRS of section 36B unless they conclude that "Congress has spoken to the precise question at issue." As should by now be amply clear, Congress has not clearly said that federal exchanges cannot grant premium tax credits. If a court finds the issue ambiguous, however, "the question for the court is whether the agency's answer is based on a permissible construction of the statute." In this situation, "legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute." As noted above, the interpretation of the ACA by the IRS is completely consistent with rather than "manifestly contrary" to the statute, and thus will be granted judicial deference.

Conclusion

In 2014 millions of your constituents will gain access to private health insurance coverage with assistance with premium tax credits. It was the hope of Congress and remains the hope of the federal agencies implementing the ACA that they will receive these premium tax credits through state exchanges. At least in the states represented by the Chairman and Ranking Member of this Committee that seems likely to be the case. But the ACA also created fallback federal exchanges, which will be available in states represented by other members of this Committee to ensure that all Americans get access to affordable health insurance. The Department of the Treasury has correctly determined based on the language and history of the ACA that premium tax credits will be available through all exchanges, state and federally facilitated. None of your constituents will be denied the tax credits made available through the ACA to ensure them access to affordable health insurance. I thank you for the opportunity to address this important issue.

References

- ¹ Jonathan Adler and Michael Cannon, Taxation without Representation: The Illegal IRS Rule to Expand Tax Credits Under the PPACA (2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2106789
- ² Families USA, Lower Taxes, Lower Premiums: The New Health Insurance Tax Credits (2010), <http://www.familiesusa.org/resources/publications/reports/health-reform/premium-tax-credits-states.html>
- ³ S 1679, <http://www.govtrack.us/congress/bills/111/s1679/text>
- ⁴ S 1796, <http://thomas.loc.gov/cgi-bin/query/z?c111:S.1796/>
- ⁵ Senate Report 111-89
- ⁶ 155 Cong. Rec. S12358.
- ⁷ 155 Cong. Rec. S13375.
- ⁸ CBO, An Analysis of Health Insurance Premiums Under the Affordable Care Act, <http://www.cbo.gov/publication/41792>
- ⁹ 155 Cong. Rec. S12107, 12/2/09
- ¹⁰ 155 Cong. Rec. S12378, 12/4/09
- ¹¹ 155 Cong. Rec. S13687
- ¹² <http://www.cbo.gov/sites/default/files/cbofiles/attachments/43472-07-24-2012-CoverageEstimates.pdf> at n. 14.
- ¹³ <http://balkin.blogspot.com/2012/07/cbo-canon-and-debate-over-tax-credits.html>,
- ¹⁴ <http://statehealthfacts.kff.org/comparetable.jsp?ind=954&cat=17>
- ¹⁵ 467 U.S. 837 (1984).

Chairman ISSA. Thank you.

I would instruct the staff to get an official copy of the that colloquy and ask unanimous consent it be placed in the record in the appropriate place.

Mr. JOST. Thank you very much, Mr. Chairman.

Chairman ISSA. Without objection, so ordered.

With that, we recognize Mr. Cannon.

STATEMENT OF MICHAEL CANNON

Mr. CANNON. Thank you, Mr. Chairman and Mr. Cummings and members of the Committee, for the opportunity to present my views on the Internal Revenue Service's final rule concerning premium assistance tax credits in the Patient Protection and Affordable Care Act.

I have submitted written testimony on behalf of my co-author, Professor Jonathan Adler of Case Western Reserve University School of Law and myself. It is our contention that this rule exceeds the IRS's statutory authority under the PPACA and is an illegal tax increase.

Two facts are key to understanding why this IRS regulation is illegal. First, both sides of this controversy acknowledge that the statutory language governing eligibility for tax credits is clear and unambiguous. The act provides that taxpayers are eligible for tax credits if they purchase a health plan through "an exchange established by the State under Section 1311." That language clearly authorizes tax credits only in State-established exchanges, and the act employs or refers to that language no less than six times when authorizing tax credits. There is no parallel language anywhere in the statute authorizing the IRS to offer tax credits through Federal fall-back exchanges established under Section 1321.

The act's authors intentionally conditioned tax credits on States establishing exchanges as one of a number of large financial incentives designed to encourage States to implement the statute. Even Professor Jost acknowledges that the provisions authorizing tax credits "clearly say," those are his words, clearly say, those credits are available solely through State-created exchanges.

Second, the remainder of the statute and the legislative history support the clear meaning of those provisions. The only statement anyone has found in the legislative history on this point comes from the bill's lead author and chief sponsor, Senate Finance Committee Chairman Max Baucus, who confirmed the bill conditions tax credits on States establishing an exchange.

And yet, contrary to the clear language of the statute and Congressional intent, this IRS regulation purports to issue tax credits in States that do not establish an exchange. Under the law's employer mandate, those illegal tax credits will trigger an illegal \$2,000 per employee tax on employers and unlawfully appropriate hundreds of billions of dollars to private health insurance companies in States that do not establish an exchange.

Since those illegal expenditures will exceed the revenues raised by this rule's illegal tax on employers, this IRS regulation will also increase Federal deficits by hundreds of billions of dollars, all contrary to the clear language of the statute and Congressional intent.

This IRS regulation is a large tax increase. It imposes a \$2,000-per-worker tax on employers and obligates taxpayers to pay for hundreds of billions of dollars of subsidies to private insurers. For every \$2 of unauthorized tax reduction that will result from this IRS regulation, it imposes \$1 of unauthorized taxes on employers, commits taxpayers to pay for \$8 of unauthorized subsidies to private insurance companies, and increases Federal deficits by \$9. Though this IRS regulation is nominally about tax credits, Government spending accounts for 80 percent of its budgetary impact.

Worse than the tax increase, though, this IRS regulation is an illegal tax increase. It lacks any statutory authority, it is contrary to both the clear language of the act and Congressional intent, and it cannot be justified on other legal grounds. It is, quite literally, taxation without representation.

As you listen to the IRS and its defenders say that this illegal tax increase is consistent with the statute or supported by the statute or recognized through the statute, notice what they are not saying. In the year since the IRS proposed this regulation, they have not cited a single statutory provision expressly authorizing the IRS to do these things in Federal exchanges, because there is no such provision. They have not cited a single statutory provision that conflicts with the language limiting tax credits to State-created exchanges because there aren't any.

Nor have they cited a single statement from the legislative history that supports either this regulation's attempt to issue tax credits and Federal exchanges or their claims that it was Congress' intent that the Patient Protection and Affordable Care Act would do so. There is simply no plausible way to argue this IRS rule is consistent with or supported by Congressional intent, much less the statute.

The most important indicator of Congressional intent is the text of the statute, itself. That text is clear. It was there for all to see before Congress approved it. It is not possible that someone who read the bill could have mistakenly thought that that language authorized tax credits and Federal exchanges.

The IRS should rescind this rule before it takes effect in 2014. Alternatively, Congress and the President could stop it with a resolution of disapproval under the Congressional Review Act.

And, finally, since this rule imposes an illegal tax on employers in States that opt not to create a health insurance exchange, those employers and possibly those States could file suit to block this rule in Federal court.

Thank you.

[Prepared statement of Mr. Cannon follows:]

Testimony of

Michael F. Cannon
Director of Health Policy Studies
The Cato Institute, Washington D.C.,

and

Jonathan H. Adler
Johan Verheij Memorial Professor of Law
Director, Center for Business Law and Regulation
Case Western Reserve University School of Law

before the

Committee on Oversight and Government Reform
United States House of Representatives

on

IRS: Enforcing ObamaCare's New Rules and Taxes

August 2, 2011

Mr. Chairman and members of the Committee, thank you for the opportunity to present our views on the Internal Revenue Service's final rule concerning "premium-assistance tax credits" under the Patient Protection and Affordable Care Act. It is our contention that this rule exceeds the IRS's statutory authority under the PPACA and is illegal.

Contrary to the clear language of the statute and congressional intent, this rule issues tax credits in health insurance "exchanges" established by the federal government. It thus triggers a \$2,000-per-employee tax on employers and appropriates billions of dollars to private health insurance companies in states with a federal Exchange, also contrary to the clear language of the statute and congressional intent. Since those illegal expenditures will exceed the revenues raised by the illegal tax on employers, this rule also increases the federal deficit by potentially hundreds of billions of dollars, again contrary to the clear language of the statute and congressional intent.

The rule is therefore illegal. It lacks any statutory authority. It is contrary to both the clear language of the PPACA and congressional intent. It cannot be justified on other legal grounds.

On balance, this rule is a large net tax increase. For every \$2 of unauthorized tax reduction, it imposes \$1 of unauthorized taxes on employers, and commits taxpayers to pay for \$8 of unauthorized subsidies to private insurance companies. Because this rule imposes an illegal tax on employers and obligates taxpayers to pay for illegal appropriations, it is quite literally taxation without representation.

Three remedies exist. The IRS should rescind this rule before it takes effect in 2014. Alternatively, Congress and the president could stop it with a resolution of disapproval under the Congressional Review Act. Finally, since this rule imposes an illegal tax on employers in states that opt not to create a health insurance “exchange,” those employers and possibly those states could file suit to block this rule in federal court.

Requiring the IRS to operate within its statutory authority will not increase health insurance costs by a single penny. It will merely prevent the IRS from unlawfully shifting those costs to taxpayers.

In a paper forthcoming in *Health Matrix*, a health law journal, we show that the IRS rule finds no support in either the statute or its legislative history.ⁱ We summarize our findings below.

Background

On March 23, 2010, President Barack Obama signed the Patient Protection and Affordable Care Act. A central objective of the PPACA is to prevail upon states to establish health insurance “exchanges” through which millions of Americans would purchase federally regulated and subsidized health plans.

The PPACA’s authors included multiple provisions designed to encourage states to establish Exchanges. Section 1311 commands that each state “shall” create an Exchange.ⁱⁱ The Act gives the Secretary of Health and Human Services the authority to make unlimited grants to states to assist them with start-up costs.ⁱⁱⁱ The Act imposes a “maintenance of effort” requirement on each state’s Medicaid program that lifts only when a state establishes a health insurance Exchange.^{iv} Section 1321 directs the Secretary to establish and operate Exchanges in states that fail to create one.^v

Consistent with these provisions, the Act authorizes the Secretary of the Treasury to issue refundable “premium assistance tax credits” through Exchanges “established by a state under Section 1311.”^{vi} There is no parallel language authorizing tax credits through Exchanges established by the federal government under Section 1321. During congressional consideration, the Act’s lead author, Senate Finance Committee chairman Max Baucus (D-MT), confirmed this asymmetry was intentional: the bill “conditions” tax credits on states establishing an Exchange.^{vii}

Both the text of the statute and Congress’ intent are thus crystal clear. The Act authorizes tax credits only in Exchanges “established by a state under Section 1311,” and withholds tax credits in states that do not establish an Exchange. The section of the law that authorizes tax credits uses or refers to that restrictive language no less than six times. The remainder of the statute supports the plain meaning of that restriction, and there is nothing in the statute that conflicts with it. The only statement anyone has found in the legislative history on this point comes from Sen. Baucus, the Act’s chief sponsor, who confirmed this was by design. The incentive that this limitation produces is consistent with numerous other incentives that Congress created to motivate states to establish Exchanges.

Since the PPACA ties additional “cost-sharing subsidies”^{viii} and penalties against employers^{ix} to these premium-assistance tax credits, the statute likewise restricts those features of the law to states that establish their own Exchanges.

IRS Rule Taxes & Spends Hundreds of Billions of Dollars without Authorization

On May 23, the IRS finalized^x a proposed rule that offers premium-assistance tax credits through Exchanges “established under section 1311 *or* 1321 of the Affordable Care Act.”^{xi} Those six characters—“or 1321”—constitute a dramatic rewriting of the statute. By issuing tax credits where Congress did not authorize them, this rule also triggers cost-sharing subsidies and imposes penalties on employers that Congress did not authorize.

According to the Congressional Budget Office, nearly 80 percent of the combined budgetary impact of these tax credits and subsidies is new federal spending.^{xii}

The total cost of this rule depends on how many states decline to establish Exchanges, a decision that many states have yet to make. In the unlikely scenario that no states establish an Exchange, Congressional Budget Office projections indicate that over the 2012-2022 period the rule’s unauthorized employer penalties would exceed \$100 billion and the budgetary impact of its unauthorized tax credits and subsidies would be on the order of \$1 trillion.^{xiii} Since the Obama administration estimates it may have to run Exchanges for as many as 30 states,^{xiv} the cost of the rule could easily reach hundreds of billions of dollars.

Federal law and certain executive orders demand heightened scrutiny of major regulatory actions. For example, the Congressional Review Act enables Congress to block major rules, which it defines as any rule with an anticipated annual cost or economic effect of \$100 million or more.^{xv} Yet the IRS concluded this rule would not have a significant economic effect.^{xvi}

The Administration’s Defense of the Rule

The administration’s public statements about this rule have been few, and are most notable for what they do not include. The administration cites no statutory authority for this move to offer tax credits in federal Exchanges—because there is no statutory authority. It likewise cites nothing from the legislative history to support its rewriting of the statute.

Instead of identifying any statutory language to support its position, the Treasury Department has said the IRS rule is “consistent with the intent of the law and our ability to interpret and implement it,”^{xvii} when in fact it is inconsistent with both the text and the intent of the law. The Department has said “[t]he statute includes language that indicates”^{xviii} that tax credits are authorized in federal Exchanges, when in fact the statute includes no such language. The Department of Health and Human Services has written that the rule is “supported by the statute”^{xix} without actually citing any part of the statute that supports it. Indeed, the administration has yet to identify any language in the PPACA that could plausibly support the IRS’s assertion of authority to provide for tax credits and subsidies in federal exchanges. The IRS has merely assumed this power for itself.

In promulgating the final rule, the IRS defended its position in the following manner:

The statutory language...of the Affordable Care Act *support[s] the interpretation* that credits are available to taxpayers who obtain coverage through a...Federally facilitated Exchange. Moreover, the *relevant* legislative history *does not demonstrate that Congress intended to limit* the premium tax credit to State Exchanges. Accordingly, the final regulations maintain the rule in the proposed regulations because it is *consistent with* the language, purpose, and structure of section 36B and the Affordable Care Act as a whole.^{xx}

Not only did the IRS fail to identify any statutory authority for its position, it also misrepresents the text and history of the PPACA. The statutory language directly contradicts the notion that the IRS can offer tax credits through federal Exchanges, as there is no language in the statute authorizing such actions. Despite the word “relevant,” which seems calculated to exclude any inconvenient aspects of the legislative history, that history clearly demonstrates that Congress intended to limit tax credits to state-created Exchanges, as we document at length in our forthcoming *Health Matrix* article. Finally, the rule cannot be “consistent” with a statute that it contradicts.

Other Defenders of the Rule

Some PPACA supporters outside the administration have offered a more detailed defense of the IRS rule, but their arguments do not support the IRS position.

Some claim that the IRS should be allowed to interpret the PPACA to authorize tax credits in federal Exchanges. Under the “*Chevron* doctrine,” courts generally defer to reasonable agency interpretations of ambiguous statutory language. Yet the relevant portions of the PPACA are crystal clear. Even the IRS rule’s most vocal defender concedes that the relevant provisions “clearly say” that tax credits are authorized only in state-established Exchanges.^{xxi} Thus defenders of the IRS rule have sought to find other parts of the law that conflict with that clear language in order to create an ambiguity that could trigger *Chevron* deference. They have focused on two passages from the statute, neither of which authorizes tax credits in federal Exchanges or conflicts with the language limiting tax credits to Exchanges established by states.

The first passage occurs in Section 1321. That section provides that if a state fails to establish an Exchange, “the Secretary shall...establish and operate such Exchange within the State.”^{xxii} Defenders of the rule claim that the words “such Exchange” refer to Exchanges established under Section 1311. Yet the statute clearly authorizes tax credits only through “an Exchange *established by the State* under section 1311.” Moreover, Section 1311 requires that for purposes of that section, “An Exchange shall be a governmental agency or nonprofit entity that is *established by a State*.”^{xxiii} (Emphases added.) Finally, Sen. Baucus’ original bill contained similar language (“the Secretary shall...establish and operate *the exchanges* within the State,” emphasis added). Yet Baucus confirmed that tax credits were available only in states that established their own Exchanges.

The second passage is an information-reporting requirement that Congress added to the PPACA through the Health Care and Education Reconciliation Act of 2010 (HCERA), more commonly known as the “reconciliation” bill Congress passed immediately after the PPACA.^{xxiv} That requirement directs all Exchanges, whether created by states (Section 1311) or by the federal government (Section 1321), to report information regarding each individual’s eligibility for tax credits, and the amount of any advance payment of those tax credits, to both the individual and to the Treasury Secretary.

This information-reporting requirement is clear and straightforward, and does not conflict with, but instead reaffirms the language limiting tax credits so state-created Exchanges. It refers to “the credit under this section” no less than four times. Since the credit authorized under that section—the new section 36B of the Internal Revenue Code—is limited to Exchanges “established by the state under section 1311,” this provision plainly requires federal Exchanges to report zero advance payments. Because it practically requires federal Exchanges to report to individuals the amount of the credit they would receive if their state were to establish an Exchange, and enables the Treasury Secretary to issue aggregate data on the tax credits that would be available to states that have yet to establish an Exchange, this provision serves the same goal as the language limiting tax credits to state-run Exchanges. Both provisions encourage states to establish an Exchange. This information-reporting requirement in no way conflicts with the plain meaning of the language restricting tax credits to state-run Exchanges.

There is simply no plausible way to argue this IRS rule is consistent with or supported by congressional intent, much less the statute. The most important indicator of congressional intent is the text of the statute itself. That text is clear. It was there for all to see before Congress approved it. It is not possible that someone who read the bill could have mistakenly thought that language authorized tax credits in federal Exchanges.

Even if—contrary to all the evidence—there had been a tacit understanding among congressional supporters that PPACA would authorize tax credits in federal Exchanges, the fact that Congress approved (and the president signed) a bill with no such authorization reveals that Congress’ *actual* intent was *not* to authorize tax credits in federal Exchanges but to enact a law without them, because the alternative was no law at all. Again, there is simply no plausible way to argue that this IRS rule is supported by the statute or congressional intent.

A Miscalculation, Not a Drafting Error

The fact that the PPACA limits tax credits, cost-sharing subsidies, and penalties against employers to states that establish an Exchange was not a drafting error. If it were an error at all, it was an error of miscalculation.

To insulate the PPACA against charges that it was a “federal takeover,” its authors sought to give states a large role in implementing its regulatory scheme, most notably by operating its health insurance Exchanges. To achieve that goal, they offered tax credits as an incentive for states to establish Exchanges.

The flip side of that incentive, however, is that the PPACA's authors literally—and *intentionally*—gave states a veto over at least three major and essential provisions of the law. They believed, of course, the risk that states would exercise this veto was small.^{xxv} But just as they misjudged the law's popularity, they miscalculated how states would respond.

Now that some experts estimate more than 30 states will decline to create an Exchange,^{xxvi} the law's authors no doubt regret their miscalculation. But that does not alter the clear meaning of the statute. Nor does it give the IRS license to rewrite a statute, impose a tax that Congress did not authorize, or borrow and spend money that Congress did not authorize.

Conclusion

The law is clear. Congress did not authorize tax credits, subsidies to private insurance companies, or penalties on employers in states with a federal Exchange. Nor did Congress grant the IRS the authority to create such credits, subsidies, and penalties, as this rule does. The Framers considered the power to tax sufficiently dangerous that the Constitution requires all revenue measures to originate in the House of Representatives, because the House is closer to the people than any other federal institution. With this rule, the IRS has put itself on a par with the Congress. It has assumed the power to rewrite a statute and alter the federal tax code.

The IRS's duty is clear. It should withdraw this rule and issue another rule that is consistent with its statutory mandate. If the agency fails to do so, Congress and the president can rescind this rule with a resolution of disapproval under the Congressional Review Act. Alternatively, employers in states that decline to create an Exchange could immediately challenge the rule in federal court.^{xxvii}

ⁱ Jonathan H. Adler and Michael F. Cannon, *Taxation Without Representation: The Illegal IRS Rule to Expand Tax Credits Under the PPACA*, HEALTH MATRIX (forthcoming), available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2106789.

ⁱⁱ Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1311, 124 Stat. 119, 173 (2010).

ⁱⁱⁱ Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1311, 124 Stat. 119, 173 (2010).

^{iv} Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 2001 (b), 124 Stat. 119, 275-276 (2010). It should be noted that there is some question whether this provision is enforceable due the Supreme Court's decision in *NFIB v. Sebelius*.

^v Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1321, 124 Stat. 119, 186 (2010).

^{vi} Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1401, 124 Stat. 119, 213-224 (2010) (Amended by the Health Care and Education Reconciliation Act).

^{vii} *Executive Committee Meeting to Consider an Original Bill Providing for Health Care Reform: Before the S. Comm. on Finance*, 111th Cong. 326 (2009), available at: <http://www.finance.senate.gov/hearings/hearing/download/?id=c6a0c668-37d9-4955-861c-50959b0a8392>; *Video: Executive Committee Meeting to Consider an Original Bill Providing for Health Care Reform: Before the S. Comm. on Finance* (C-SPAN broadcast Sept. 23, 2009), at 2:53:21, <http://www.c-spanvideo.org/program/289085-4>.

Senator Ensign: Is this bill, the underlying premise in this bill that...we are making states change their laws, their coverage laws? Aren't we doing that? And so why would not most of the coverage rules in this bill, underlying bill, be...only in the jurisdiction of the HELP Committee and not in the jurisdiction of this committee?...On certain minimum plans, exchanges. All those coverage things are state laws...How do we have jurisdiction over changing state laws on coverage?...

The Chairman: There are conditions to participate in the Exchange.

Senator Ensign: That is right.

The Chairman: For setting up an Exchange.

Senator Ensign: These would be conditions to participate—

The Chairman: And states—an Exchange is, essentially is tax credits. Taxes are in the jurisdiction of this committee.

^{viii} Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1402, 124 Stat. 119, 223 (2010).

^{ix} Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1513, 124 Stat. 119, 253-256 (2010) (Amended by the Health Care and Education Reconciliation Act of 2010).

^x Department of the Treasury, Internal Revenue Service, *Health Insurance Premium Tax Credit*, 77 FEDERAL REGISTER 30377 (May 23, 2012), available at: <http://www.gpo.gov/fdsys/pkg/FR-2012-05-23/pdf/2012-12421.pdf>.

^{xi} Department of the Treasury, Internal Revenue Service, *Health Insurance Premium Tax Credit*, 76 FEDERAL REGISTER 50934 (Aug. 17, 2011), available at: <http://www.gpo.gov/fdsys/pkg/FR-2011-08-17/pdf/2011-20728.pdf> (emphasis added).

^{xii} Congressional Budget Office, unpublished data. (Available on request from the authors.)

^{xiii} CONGRESSIONAL BUDGET OFFICE, ESTIMATES FOR THE INSURANCE COVERAGE PROVISIONS OF THE AFFORDABLE CARE ACT UPDATED FOR THE RECENT SUPREME COURT DECISION (2012), available at: <http://www.cbo.gov/sites/default/files/cbofiles/attachments/43472-07-24-2012-CoverageEstimates.pdf>.

^{xiv} J. Lester Feder, *Sebelius: Exchange funding request was anticipated*, POLITICO PRO, Feb. 14, 2012, <https://www.politicopro.com/go/?id=9220> [subscription only] (“We don’t know if we’re going to be running an exchange for 15 states, or 30 states.”).

^{xv} See 5 U.S.C. § 804 (2).

^{xvi} See Department of the Treasury, Internal Revenue Service, *Health Insurance Premium Tax Credit*, 77 FEDERAL REGISTER 30385 (May 23, 2012), available at: <http://www.gpo.gov/fdsys/pkg/FR-2012-05-23/pdf/2012-12421.pdf> (“It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866, as supplemented by Executive Order 13563. Therefore, a regulatory assessment is not required”).

^{xvii} Sara Hansard, *Private Exchanges Could Impact Success of State Exchanges*, BNA HEALTH INSURANCE REPORT, Oct. 26, 2011.

^{xviii} Letter from Douglas H. Shulman, Commissioner, Internal Revenue Service, to David P. Roe, Representative, U.S. House of Representatives (Nov. 29, 2011), http://roe.house.gov/UploadedFiles/IRS_Response_to_letter_on_PPACA_Exchange.pdf.

^{xix} CENTERS FOR MEDICARE AND MEDICAID SERVICES, CENTER FOR CONSUMER INFORMATION AND INSURANCE OVERSIGHT, STATE EXCHANGE IMPLEMENTATION QUESTIONS AND ANSWERS 8, (November 29, 2011), available at: http://cciio.cms.gov/resources/files/Files2/11282011/exchange_q_and_a.pdf.pdf.

^{xx} Department of the Treasury, Internal Revenue Service, *Health Insurance Premium Tax Credit*, 77 FEDERAL REGISTER 30378 (May 23, 2012), available at: <http://www.gpo.gov/fdsys/pkg/FR-2012-05-23/pdf/2012-12421.pdf> (Emphases added).

^{xxi} Timothy S. Jost, *Yes, the Federal Exchange Can Offer Premium Tax Credits*, HEALTH REFORM WATCH, Sept. 11, 2011, <http://www.healthreformwatch.com/2011/09/11/yes-the-federal-exchange-can-offer-premium-tax-credits/>.

^{xxii} Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1321, 124 Stat. 119, 186 (2010).

^{xxiii} Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1311 (d), 124 Stat. 119, 176 (2010).

^{xxiv} Health Care and Education Reconciliation Act, Pub. L. No. 111-152, Sec. 1004 (c), 124 Stat. 1029, 1035 (2010) and the Patient Protection and Affordable Care Act, Pub. L. No. 111-148, Sec. 1401, 124 Stat. 119, 219 (2010).

^{xxxv} Supporters of the PPACA confidently predicted all states would establish Exchanges. Prior to enactment, Secretary of Health and Human Services Kathleen Sebelius testified that states were “very eager” to create Exchanges and predicted most would do so quickly. *Departments of Labor, Health and Human Services, Education, and Related Agencies Appropriations for 2011: Hearing Before the H. Comm. on Appropriations*, 111th Cong. 170-171 (Mar. 10, 2010), available at: <http://www.gpo.gov/fdsys/pkg/CHRG-111hhrg58233/pdf/CHRG-111hhrg58233.pdf>. Shortly after enactment, President Obama predicted, “by 2014, each state will set up what we’re calling a health insurance exchange.” Barack Obama, U.S. President, Remarks on Health Insurance Reform in Portland, Maine (Apr. 1, 2010), available at: <http://www.whitehouse.gov/the-press-office/remarks-president-health-insurance-reform-portland-maine>.

^{xxxvi} J. Lester Feder and Jason Millman, *Few States Set for Health Exchanges*, POLITICO, May 21, 2012, <http://www.politico.com/news/stories/0512/76596.html> (“Many insurance experts and health policy consultants predict only a dozen or so states will be ready to run exchanges on their own — and a few say that projection may be too sunny”).

^{xxxvii} In light of the Supreme Court’s ruling in *NFIB v. Sebelius*, a strong case can be made that the Anti-Injunction Act would not delay employers’ ability to establish standing to challenge the IRS rule.

Chairman ISSA. I thank the gentleman.

I now ask unanimous consent that our colleague, the gentleman from Tennessee, Dr. Roe, be allowed to participate in today's hearing.

Without objection, so ordered.

I will now recognize myself for a round of questioning.

Professor Jost, is it undeniable that there is a cost difference between all States participating, some States participating, and the Federal Government essentially preempting the States choosing not to participate? In other words, if only 14 States participate, our scoring shows over half a trillion dollars less in cost to the Federal Treasury. Would you disagree with that?

Mr. JOST. I would agree that citizens of all the rest of the States would be denied a—

Chairman ISSA. Okay. So I will take that as yes, it is a half a trillion dollars to the taxpayers or, more specifically, half a trillion dollars we don't borrow from the Chinese.

Mr. JOST. Well, a half a trillion dollars that would not be granted in Federal tax credits to citizens of this Country. Yes. Thank you.

Chairman ISSA. Mr. Cannon, when CBO scored this, my understanding is they made the assumption that all States would participate. Is that your understanding?

Mr. CANNON. There is a widespread assumption when this law was passed all States would establish exchanges.

Chairman ISSA. Okay. But States not participating has a ramification. Isn't it true that a State not participating means that a company would not get a \$2,000 penalty plus the cost of the subsidy in that case if there is no State exchange?

Mr. CANNON. That is correct. What triggers the penalties against employers under this law's employer mandate, is when one of their employees receives a tax credit through an exchange, if there are no State-created exchanges there would be no tax credits. If there are no tax credits—

Chairman ISSA. So let's run through, because I now understand why Justice Roberts made the decision he made. Clearly this was a pot full of taxes. We may disagree with whether it was right, but I begin to see why this is all about taxing, that ObamaCare is all about taxing. So let me ask a question. Under a State that does not create an exchange, does the individual still have an individual mandate?

Mr. CANNON. Yes.

Chairman ISSA. Does the individual then have to seek either private insurance or the Federal exchange that is anticipated in the law?

Mr. CANNON. Or pay a penalty tax.

Chairman ISSA. okay. So the Supreme Court decision that my colleague, the Ranking Member, referenced doesn't change. The States have the right to opt out under this law. They have chosen to do so in huge amounts, or at least not to participate, and it doesn't change anything related to the Supreme Court question of the individual mandate; is that correct?

Mr. CANNON. That is correct.

Chairman ISSA. So the challenge at the Supreme Court, which will occur when the tax is implemented, essentially the first time

an employer gets his bill he can then make a challenge that will go all the way to the Supreme Court, what would be an all new challenge that won't occur until 2015, correct?

Mr. CANNON. That is actually not clear, sir. Employers could file suit today, and it is a defensible, I think, perhaps the correct reading of the Supreme Court's ruling in *NFIB v. Sebelius* that the anti-injunction act might not bar an employer establishing standing immediately.

Chairman ISSA. But certainly it didn't bar on the other tax. But you would say, and I think since Professor Jost only wants to answer the questions he wants to answer, not the ones I ask, clearly this is a separate issue that will very possibly go all the way to the Supreme Court; is that correct?

Mr. CANNON. I can't say how far it would go, sir.

Chairman ISSA. Let me rephrase that. This is a separate issue which would be eligible?

Mr. CANNON. That is correct.

Chairman ISSA. Okay. Ms. Olson, you mentioned in our earlier conversation, I hope you don't mind my bringing it up, that your legal counsel, your general counsel, had made this decision from the rule. Correct?

Ms. OLSON. It is the Internal Revenue Service chief counsel, not mine, yes.

Chairman ISSA. Right, but yours being the IRS.

Ms. OLSON. Yes. Correct.

Chairman ISSA. That is a political appointee, isn't it?

Ms. OLSON. Well, yes it is.

Chairman ISSA. Okay. So a political appointee made the decision that this rule should be made without, according to Mr. Cannon and my reading of the bill, without any legal standing. I'm going to ask you another question. This one concerns me more. In year 2010 report you wrote, "The new W-2 reporting requirements has raised numerous concerns that reporting the value of health insurance on employees' W-2 may cause the amount to be taxed." You wrote that.

You also, in your 2010 report, which is in the record, you said, "To get to the underlying goal of the new law, health coverage for the vast majority of Americans," and this was a question, "Will the IRS audit every taxpayer who does not report?" These are areas of concern you raised.

Ms. OLSON. Yes.

Chairman ISSA. Let me go through this. You raised it again. If you don't audit every single person to make sure that they properly were taxed, then we have a vast hole in which there could be subsidies paid that shouldn't, there should be individual fines, taxes, if you will, \$2,000 for those who don't. So essentially you almost have gotten into a situation in which every American needs to be audited every year. That is more or less what you are saying there.

Ms. OLSON. Sir, the first quote we were saying there is confusion about taxpayers when they get information on their W-2 reporting what their premiums are, should that be taxed, and the answer is no, that is not being taxed.

Chairman ISSA. Sure, I understand you can explain part of it, but the other part is essentially, if you don't audit every American every year, then this thing won't be right?

Ms. OLSON. The second issue was we were raising that as a concern, and if the IRS takes its normal approach, which is to select portions of the population to audit on any tax position, then you are not going to be able to effectively implement the mandate.

Chairman ISSA. Okay. And I want to recognize the Ranking Member, but I just want to make it clear it appears that the Commissioner made a political decision, which was the new W-2 reporting requirement has been delayed until after this Presidential election, hasn't it?

Ms. OLSON. I can't speak to that. I think the Commissioner is on the next panel.

Chairman ISSA. Well, no.

Ms. OLSON. There has been a delay.

Chairman ISSA. There has been a delay, and the effect of that delay has been it won't appear for people to see until after this election.

Ms. OLSON. That is a matter of fact. Yes.

Chairman ISSA. Okay. With that, I recognize the Ranking Member.

Mr. CUMMINGS. To all of our witnesses, I really want to see this law implemented to its fullest degree, because I know that right now, right this second, there are people watching us. There is somebody leaning in a sick bed that can't get up. There is somebody who cannot get insurance. And they are saying, you know, whatever you do, whatever arguments you have got, get them straight because I want to live. And I want to speak for them because they are out there.

I have often said that we all are the walking wounded. All of us are the walking wounded, and we are walking yet and wounded we will be. So, Ms. Olson, in your testimony you are generally positive about what the IRS has accomplished to date, and you say that over the past two years the IRS has used its time well, and I am going to come back to you in a moment.

Mr. EVERSON, I want to thank you for your balanced testimony, but I want to ask you this. You were IRS Commissioner. We can do this. We can get this done. I know you highlighted a lot of issues that we need to be aware of, and I really appreciate that, and you are talking about some things that are perhaps preventive, hopefully, that is, so the IRS won't run into this, but we can get this done, can't we? This is America. This is the United States. We are a can-do Nation.

Mr. EVERSON. Let me say this, sir. It is quite possible we will get it done. The Service is going to do its level best. The Commissioner, when you ask the Commissioner this question, he is going to say yes, of course. He has to. His job is to implement the law, however strong or however flawed, so that he can't be then before the Committee or before Ways and Means or Finance and have people say, well, you never liked this law. You said you couldn't do it anyway. So the Service is always going to say yes.

I think the Service in this instance is a little bit like that frog they always talk about in the frying pan that you keep turning up

the heat until sooner or later the frog is dead. It doesn't jump out. And that is my worry here, that there are so many pieces, there are so many things to do, especially on the systems side, as has been indicated, on the reg side. There is so much confusion out there that I do worry about this.

And then secondly, as you and I have discussed, I worry about the impact on tax administration from a failure here.

Mr. CUMMINGS. Yes.

Mr. EVERSON. So I don't think this is going to be easy and I don't think it is a certainty that it can be done, sir.

Mr. CUMMINGS. You said what? What was the last statement?

Mr. EVERSON. I don't think it is easy and I don't think it is, by any means, a certainty that it can be done, even with very strong efforts by the IRS.

Mr. CUMMINGS. And with resources. I think that was one of the things that you talked about.

Mr. EVERSON. Resources. As I have indicated, absolutely, give the Service the resources it needs to do then if you are going to hold them accountable for doing it.

Mr. CUMMINGS. Thank you.

Ms. Olson, you raised one specific challenge, and that was the need for a communications plan and taxpayer education efforts. Why is that so important? I agree with you, by the way. I think that is much needed.

Ms. OLSON. We need to tell taxpayers, make sure taxpayers know where they should go for each step of this program, and that for the advanced premium credit they are dealing with the exchanges, for issues on the tax return they are dealing with the IRS. They need to update their information during the year so they don't get socked with a tax at the end of the year. And so we were talking about changing behavior, and we really need to communicate that information out there.

To something else that Former Commissioner Everson said, you know, about the burden on the CPAs and other return preparers, I think we need to start talking to them about what to expect as we get closer to this date.

Mr. CUMMINGS. I don't know if you have read the GAO reports on the implementation of the Affordable Care Act, but they are also generally positive, Ms. Olson, about the IRS efforts to date. GAO finds that top IRS leaders have been directly involved in this process, and that IRS has accomplished a number of those, and that the risk of being identified and analyzed at the individual project level.

GAO also makes a number of specific recommendations to improve the implementation of the program. For example, GAO recommends that IRS develop an integrated plan with detailed cost estimates and develop procedures identifying and evaluating risk mitigation strategies. Ms. Olson, are you aware of GAO's findings? Are they consistent with yours?

Ms. OLSON. Yes. And the IRS I know has responded to GAO's findings and is taking steps to address that.

Mr. CUMMINGS. Now let me ask you about another report. This one is from the Treasury Inspector General for tax administration and it is also fairly positive. It says that the IRS is effectively using

tracking systems to monitor implementation, that it is working on forms and publications and other consumer outreach, and that it has completed plans for computer programming tasks.

And overall the Inspector General says this: the appropriate plans have been developed to implement tax-related provisions of the ACA using well-established methods for implementing tax legislation. Do you agree or disagree with the IG's conclusion?

Ms. OLSON. From what I have seen, I would have to agree to date.

Mr. CUMMINGS. Well, my goal on this Committee is to conduct a constructive oversight and to work with you and the IRS to flag potential issues before they become problems. We will be having the IRS Commissioner on the next panel and I am looking forward to his thoughts, and I am hoping that he has listened very carefully to what Mr. Everson has just said and don't tell us what he thinks we want to hear but tell us what we need to hear.

With that I yield back.

Chairman ISSA. I thank the gentleman.

We now recognize the distinguished gentleman from Tennessee, Dr. DesJarlais, for his questions.

Dr. DESJARLAIS. Thank you, Mr. Chairman.

What we need to decide today is whether the IRS bypassed Congress, in a sense wrote a new tax law that is a power given solely to Congress, so let's go through first a series of yes/no questions. I know panels tend not to like those, but let's try to do the best we can.

First, Mr. Cannon, is there anything stopping the IRS from implementing Section 36(b) of the Internal Revenue Code exactly as written?

Mr. CANNON. Section 36(b) is large and complicated, sir. If what you mean is the provision restricting tax credits and State-run exchanges, no.

Dr. DESJARLAIS. Professor Jost?

Mr. JOST. Section 36(b), as I explained, if you read the definitions, does authorize Federal exchanges to issue a tax credit, so no, there is no problem.

Dr. DESJARLAIS. There is no problem. Thank you.

In one part of the law it authorizes tax credits for people who purchase a qualified health plan through an exchange established by a State under Section 1311, and even people who defend the IRS on this issue, such as yourself, Professor Jost, say that this part of the law is clear. Is there any part of the statute that prevents you from doing just that, offering tax credits only in State-run exchanges?

Mr. JOST. Again, the definitions.

Dr. DESJARLAIS. Mr. Cannon, is there any part of the statute that prevents you from doing just that, offering tax credits?

Mr. CANNON. No.

Dr. DESJARLAIS. No. Okay.

Mr. CANNON. No. In fact, the statute requires that.

Dr. DESJARLAIS. Okay. Is there any part of the statute that conflicts with that, Mr. Cannon?

Mr. CANNON. No. In fact, all other elements of the law support the clear meaning of that limitation of tax credits to health insur-

ance exchanges established by the State under Section 1311, and established by the State. Those words are key.

Dr. DESJARLAIS. What about the information reporting requirement?

Mr. CANNON. That does not conflict. It does require exchanges established under Section 1321 by the Federal Government to report information related to eligibility for tax credits and the advanced payment of tax credits to the Treasury Secretary and to individuals enrolled through those exchanges.

Dr. DESJARLAIS. Okay.

Mr. CANNON. But that does not conflict in any way with the limitation of tax credits to State-run exchanges.

Dr. DESJARLAIS. Okay. So what is stopping the IRS from implementing the tax credit provision exactly as written and exchanges from implementing the information reporting requirement exactly as written, or can they both be implemented exactly as written without conflicting with each other?

Mr. CANNON. The latter. They can both be implemented exactly as written without any conflict.

Dr. DESJARLAIS. Agreed, Professor Jost?

Mr. JOST. I would agree because, again, Federal exchanges can issue premium tax credits and can report.

Dr. DESJARLAIS. Okay. Do you agree that when authorizing these premium assistance tax credits Internal Revenue Code explicitly refers to only health insurance exchanges as established by the States under 1311, Professor Jost?

Mr. JOST. I do, and, again—

Dr. DESJARLAIS. Mr. Cannon?

Mr. JOST.—given the definition, that means Federal exchanges.

Mr. CANNON. That is what the statute says, but I would disagree with Professor Jost that the Federal Government can establish a health insurance exchange established by the State, which is what Section 1311 requires. And that claim is completely inconsistent with the text of the law.

Dr. DESJARLAIS. Simple question: do you agree that when authorizing those tax credits the IRC reportedly refers to exchanges established by the State under 1311?

Mr. CANNON. That is correct.

Dr. DESJARLAIS. Professor Jost, do you agree with that?

Mr. JOST. Again, given the definition that includes Federal exchanges.

Dr. DESJARLAIS. Okay. Do you agree that the ruling providing tax credits in Federal exchanges will trigger penalties against employers under the employer mandate in States with Federal exchanges, Professor Jost?

Mr. JOST. If they do not offer health insurance or adequate or affordable insurance and their employees go into the exchange and get Federal premium tax credits, yes.

Dr. DESJARLAIS. Mr. Cannon, yes or no.

Mr. CANNON. Yes.

Dr. DESJARLAIS. Thank you. Are you aware, Professor Jost, of how many time state reconciliation bill, the Health Care and Education Act, amends Section 1401 of the ObamaCare law which cre-

ated IRC Section 36(b) authorizing the tax credits in State-created exchanges?

Mr. JOST. Well, at least once, but I don't know off the top of my head.

Dr. DESJARLAIS. Seven times. Are you aware of how many times that the same reconciliation bill amended Section 1402 of the Affordable Care Act which authorizes cost-sharing subsidies, credits in State-created exchanges?

Mr. JOST. Not off the top of my head.

Dr. DESJARLAIS. Okay. Five times. So a total of 12 times. So if Congress intended to offer tax credits and cost-sharing subsidies through Federal exchanges, then why didn't Congress include any language to that effect among the 12 amendments within the reconciliation bill authorizing tax credits and cost-sharing subsidies through exchanges established by U.S. territories? Is that a coincidence?

Mr. JOST. Again, it had already authorized Federal exhibits to issue tax credits, and therefore there was no need to amend it.

Dr. DESJARLAIS. Mr. Cannon, do you agree? Is he going wrong here?

Mr. CANNON. There is no language authorizing tax credits in Federal exchanges, and the claim that Professor Jost is making is not supported by the text. What he is saying is that the Federal Government can create a health insurance exchange for purposes of Section 1311, but Section 1311, itself, clearly says that, for purposes of that section, "an exchange shall be a Governmental agency or nonprofit entity that is established by a State." It is simply implausible to argue that the Federal Government can establish an exchange that is established by a State.

Dr. DESJARLAIS. In fact, we know it was their intent to entice or almost coerce States into signing up for these exchanges. They thought that when ObamaCare was released the States would just line up and sign up for these exchanges, but when they didn't they realized they had a real problem. But the intent of the bill was clear. That is what they were trying to do. Do you agree?

Mr. CANNON. And that intent was revealed by the Senate Finance Committee, the Chairman Max Baucus. When challenged by opponents of the bill in his Committee he said that it does condition tax credits on the State creating an exchange.

Chairman ISSA. The gentleman may finish the answer if he wants. You did?

Mr. CANNON. Yes.

Chairman ISSA. The gentleman's time is expired. Thank you.

We now go to the gentleman from Illinois, Mr. Davis, for his questions.

Mr. DAVIS. Thank you very much, Mr. Chairman. I want to thank the witnesses for appearing also.

Ms. Olson, opponents of health reform legislation have unfairly characterized the Affordable Care Act as resulting in "an unprecedented expansion of the IRS powers." To be honest, I am not exactly sure of what they are talking about, so let's look at some of the possibilities.

One claim they appear to be making is that the IRS has the new authority to distribute billions of dollars in tax credits to individ-

uals purchasing health insurance on the exchanges. I think that is a good thing, but it seems that some of my colleagues on the other side of the aisle do not. Ms. Olson, does this aspect of the Affordable Care Act represent an unprecedented expansion of the IRS powers? Or does the IRS have decades of experience with distributing funds as part of similar social programs, like when the IRS distributed the Bush Administration's economic stimulus payment?

Another claim that opponents of the law are making is that the IRS will have access to individuals' personal health information when they are verifying insurance coverage.

Are these accurate assertions?

Ms. OLSON. I view ACA not as an unprecedented expansion of IRS powers, but rather an unprecedented expansion of IRS work. The powers that we have in the law are powers that reside in tax administration, period. We implement the earned income tax credit, which is billions of dollars; the first-time homebuyer credit; as you referenced, the economic stimulus payment. We are a disperser of payments, and that trend has been happening since the 1970s.

In terms of health information that we would get, my understanding is that we would get the information from insurers whether or not the taxpayer was covered, and essentially nothing else. The amount of the premium paid. And that would be it. Nothing about their state of health or anything like that. That is new information that we will be getting; however, we have always been getting information from third parties. So it is not a new approach giving us information; it is new information.

Mr. DAVIS. Well, let me proceed. A number of people appear to still believe that the IRS will be subjecting individuals to liens or levies or even jail time if they fail to purchase insurance. Is this from your analysis?

Ms. OLSON. No. The law, at my urging, in fact, prevents the IRS with respect to the individual mandate, what people call the individual mandate, the IRS is prevented from issuing liens or levies or its other enforcement action. It can collect that mandate through what we call refund offset, where a taxpayer has a refund coming to them and we would offset that refund amount with the amount of the penalty.

Mr. DAVIS. And if low-income taxpayers cannot afford health insurance, will they be subject to a penalty?

Ms. OLSON. There are many provisions in the law allowing for exemptions, both for hardship, and the mandate only applies to taxpayers starting at a certain level of income.

Mr. DAVIS. Some folks have claimed that the Affordable Care Act will require the IRS to hire 16,000 new enforcement agents. The Commissioner has said on a number of occasions that this is a made-up number with no basis in fact. Is this your understanding, perhaps, as well?

Ms. OLSON. I think the Commissioner can certainly speak on the next panel about this. The internal conversations, my understanding is that we are maybe looking at, going forward, 800, 860 full-time equivalents for doing this work once it is implemented.

Mr. DAVIS. Thank you very much. My time has expired. Mr. Chairman, I yield back.

Chairman ISSA. I thank the gentleman.

I now ask unanimous consent that Professor Jost's September 11, 2011, article, Yes, the Federal Exchange Can Offer Premium Tax Credits be placed in the record.

Without objection, so ordered.

Chairman ISSA. Professor Jost, my staff has asked me to give you an opportunity to clarify an answer you gave to Dr. DesJarlais. You said that it was in the act, in the September 11th you said it was a drafting error. Can you reconcile? Is it in the act in written language, or in your September 11, 2011, article were you correct that it was, in fact, clearly left out of the act?

Mr. JOST. I have learned over the last year a bit more about the statute, and that is something that I think is worth doing.

Chairman ISSA. I just want to—

Mr. JOST. I think the statute could have been better drafted, but I think if you read the statute as a whole, including the definitions, it does authorize Federal exchanges and I was wrong at that point.

Chairman ISSA. Okay. So you are saying 2011 is incorrect, the article, and you now stand by your testimony?

Mr. JOST. That part of the 2011 article was incorrect, and I now stand by my testimony. Thank you.

Chairman ISSA. Thank you very much.

We now recognize the gentleman from Michigan, Mr. Walberg.

Mr. WALBERG. Thank you, Mr. Chairman.

I think the insertion of the music at that proper time was probably coming from the Sovereign of the Ages saying that we are living in a fantasy world that this thing is going to work, and so maybe that music will come in again at some time.

As I understand from what I hear and what I read, what I have heard today, that tax credit eligibility and size are determined by a formula that includes a number of things, details. The tax credits are sent directly from Treasury to health insurance companies.

Ms. Olson, you have stated that "taxpayers who did not update their household information during the year may find that they owe a significant amount of money at the end of the year. Money they likely do not have." I would concur with you on that statement. At least my concerns would concur with you. What type of information will households have to update?

Ms. OLSON. If they are determined by the exchange in advance that they are eligible for these advance payments of their health care premium, they will need to let the exchanges know if they have gotten an increase in salary, because that may make them ineligible for the full amount of credits that they are getting. On the other hand, if they have a child may become ineligible in their household, someone may die in their household. On the other hand, they may be entitled to more credit if they get unemployed or something like that.

But the point is it is the changing of their circumstances that they are going to have to update it during the year, and that they could end up owing money at the end of the year is a risk and I am very concerned about that.

Mr. WALBERG. And even with different States, changing States, as many people have to do just to find a job now, changing States with different provisions in their exchanges could make it very difficult, as well?

Ms. OLSON. It could very well be.

Mr. WALBERG. You know, I come from the aspect if you are a person who has to file a quarterly report, you understand the complexities of that. But if you have a bunch of new citizens who are going to be really required, if they are going to be intentional about it and not run amuck, are going to be filing reports that they have never done before and don't have the abilities of external resources to help them. The challenge will be there. Do you believe that most Americans are going to update the IRS or State exchanges when they change jobs, get married, move States, whatever?

Ms. OLSON. I think it is going to be a very great learning curve.

Mr. WALBERG. With a lot of pitfalls.

Ms. OLSON. With a lot of pitfalls. The only saving grace is about 80 percent, 75 to 80 percent of taxpayers get a refund, so it is unlikely that they will owe money to the IRS. It is just that their refund, average refund is \$3,000, at least the first year their refund might be, you know, decreased. I am not minimizing that. That is a significant thing for taxpayers.

Mr. WALBERG. And the confusion, especially the first reconciliation in 2015, how would you describe it?

Ms. OLSON. I think it will be a surprise to the taxpayers if they don't update their information.

Mr. WALBERG. And persons who are in a situation where they are now having to use a Government-run or Government takeover of health care are not only going to have the sickness and the problems that they have, but also the confusion, the frustration, the worry, in some cases the terror of trying to deal with all of this while they are trying to get well.

Ms. OLSON. I think the agencies are trying to make it as easy as possible.

Mr. WALBERG. Okay. Thank you for your responses.

Mr. EVERTON, many experts point out that the tax credit most similar to ObamaCare's premium tax credits is the earned income tax credit. Unfortunately, the ITC has an extremely high error rate and fraud rate, sadly. What lessons are there from the ITC experience and IRS that the IRS can take to reduce the error rate and fraud rate with premium credits?

Mr. EVERSON. Well, the program, sir, is very complex, and it is distinguished from many other Federal programs where there is a real front-end application process where you sort of sort through information and then someone is deemed ineligible or eligible for a benefit, but there is no administrative cost to the ITC in the sense that most big food stamps or other Federal programs they have got a 6 or 7 percent monies that are appropriated go to administering on the front end. The ITC is, by and large, like other things on your return. You put it out there, and then if the Service has questions—and they hold a lot of the returns before they pay, because, as you indicate, there is a lot of fraud, there is a lot of just plain misunderstanding—even more of that—that gets in there, and that is a real problem. But I would say the biggest piece is the complexity and the—

Mr. WALBERG. So ObamaCare is more complex than the ITC and other—

Mr. EVERSON. I agree with the advocate's comments earlier that it is about a lot more work, but it is about also very great complexity within each of the many provisions that are in the statute. So I consider this comparable in many ways, yes, I do, to the EITC. The EITC, at least when I was Commissioner, had the highest error rate of any Federal program. I believe it still does. I don't know.

Mr. WALBERG. And this is more complex?

Mr. EVERSON. Yes. I think it is.

Chairman ISSA. Would the gentleman yield for just one second?

Mr. EVERSON. I would yield.

Chairman ISSA. I just want to verify, Ms. Olson. You were saying individual taxpayers would have to update their record if they had a change. What year will be used by the IRS initially to determine, in 2014, what the subsidy will be? I don't want an open question. I just want to make sure it is clear.

Ms. OLSON. The 2012 income is what is used to determine your eligibility for a premium, advanced premium payment, for 2014.

Chairman ISSA. Thank you. I just wanted to make sure we got that in the record. I thank the gentleman.

With that, I recognize the gentleman from Massachusetts for five minutes.

Mr. TIERNEY. Thank you, Mr. Chairman. I thank all of our witnesses today for their testimony and for their knowledge on this thing.

Professor Jost, I just wanted to ask a question about the fact that until recently a lot of the insurance companies were spending, I believed, a significant amount of their premium money on things other than health services, whether it be salaries or bonuses or lobbyists or other administrative costs. One study, in fact, indicated that ten of the largest insurance companies saw their profits jump some 250 percent between 2000 and 2009. In just 2009, alone, at the height of the economic recession, the five biggest insurance companies saw their profits increase by 56 percent. So I find that a startling figure, but I wonder if you have any idea how these health insurance companies were able to increase their profits so dramatically during that time.

Mr. JOST. Yes, I do. The medical trend, the growth in health care costs, has been growing at historically low levels for the last two or three years; nevertheless, insurance companies were increasing premiums because they believed that, once the recession ended, people would start using more medical care and trend would go back up. So there has been a growing gap between premiums and actual health care costs.

The medical loss ratio 80/20 rule that the Affordable Care Act imposes has resulted in 12.8 million Americans receiving \$1.1 billion in rebates that were due as of yesterday, including \$300 million in rebates for American small businesses. Yet, insurance companies are still doing very well. I was just reading this morning Carl McDonald says that Cigna beat expectations and that most insurance companies in their most recent quarterly reports that were just issued beat expectations. So we have a solution where premiums are coming down, Americans are getting rebates, insurers are still doing just fine.

Mr. TIERNEY. Thank you. You know, I am glad to hear that. I was responsible for putting that provision in the House bill when it went through the education hearings on that, and this is the expected, anticipated result that we thought, and so it is good to know that your remarks coincide with what the Secretary has told us, as well, and what I think a number of reports have done that.

Professor Jost again, the IRS issued their final regulation allowing the premium tax credits to be available to all people, regardless of the origin of their exchange participation; is that right?

Mr. JOST. That is correct.

Mr. TIERNEY. Okay. So Mr. Cannon made his argument that the rule constitutes a net tax increase. I assume that you don't agree with him on that?

Mr. JOST. No. This is a tax cut.

Mr. TIERNEY. And under the interpretation of the Affordable Care Act that Mr. Cannon puts forward, residents of States with Federally operated exchanges wouldn't qualify for the premium assistance tax credits, so I want to give you another opportunity, just rather than passing your opening remarks on that, to explain what the cost of Mr. Cannon's interpretation would be to taxpayers who do not get their tax credits.

Mr. JOST. Well, it is hard to know exactly. I mean, there are going to be a trillion dollars in tax credits over ten years, and it looks like initially probably 30 or 40 States are going to have Federal exchanges, so all of the residents of those States would be denied premium tax credits.

Mr. TIERNEY. So the National Health Interview Survey just released this past Tuesday says that more than one in five middle-aged United States adults and nearly half of the adults over the age of 65 have more than one chronic health condition, whether hypertension, diabetes, things of that nature. There are more and more people every day that need assistance in managing and preventing those diseases, and yet 50 million people are without access to health insurance.

So, Professor, can you explain what the impact will be on those individuals of the exchanges coming into effect in 2014?

Mr. JOST. Well, a report done by the Harvard Medical School a couple of years ago projected that about 45,000 Americans die every year because they are uninsured. Making premium tax credits available to 20 million Americans so that they can afford health insurance is really a question of life and death. It is going to be Americans whose lives are saved because they can get premium tax credits, and in many States that means initially premium tax credits through the Federal exchange.

Mr. TIERNEY. Thank you.

I yield back, Mr. Chairman.

Chairman ISSA. I thank the gentleman.

We now go to the gentlelady from New York, Ms. Buerkle.

Ms. BUERKLE. Thank you, Mr. Chairman, and thank you for this very important hearing. And thank you to our panelists for being here today.

I graduated from nursing school a very long time ago. I was one of those diploma grads who spent time doing clinical nursing. And then when I was 40 I decided to go to law school, and for 13 years

before I came to Congress I represented a large teaching hospital in upstate New York. So pretty much my professional career has been spent in health care, and one of the reasons I ran for Congress was because I thought the direction of the Affordable Care Act was incorrect.

Now I do want to make one point, and that is my colleague on the other side of the aisle mentioned we are opposed to health care reform. By no means are we opposed to health care reform. But I would have thought, in a health care reform and in a Nation that wants to make sure people have increased access to health care, decrease the cost of health care, that we would have seen tort reform, that we would have seen the increased use of health savings accounts, that we would have seen the ability to buy insurance across State lines. Portability. Increasing the number of physicians and encouraging them to go into the family practice and the internal medicine fields.

But we don't see any of that, and I sit here and I think, Have we lost our way so much in this city that when we talk about health care reform we have to bring in the IRS and talk about raising taxes on the American people by \$500 billion? Who in their right mind thinks that what we are talking about here today is going to increase access to health care for the American people or decrease the cost? Who has gotten so far away from reality down here that they think this is the way we help the American people?

When my colleague talks about that patient laying in his bed needing health care, if you think that going to the IRS and dealing with the IRS is going to increase your health care, your access to health care, or decrease the cost or improve the quality of health care in this Nation, we have a problem in the United States of America.

I am sitting here stunned. I have paid such close attention to this. All of my colleagues have. And I sit here and I think, What in God's name are they talking about and how is that going to help that senior citizen understand her benefits, make sure she is covered, make sure that person who is unemployed has access to health care. This is gibberish. We are talking about the most intensely personal issue for the American people, health care. Health care is so important to every person in this room. It affects how they live their lives. And we are talking about an agency, the IRS, and I know firsthand from the complaints that come in to my office how difficult it is to deal with the IRS, how unresponsive the IRS is, and now you take the IRS and it is not just going to be your income tax any longer, it is going to be, well, I have had a baby, I have lost my job, I have gotten a promotion. All that now has to be communicated to the IRS.

The American people and this health care system that has been created in the Affordable Care Act, the largest tax on the American people in the history of this Nation, if one person can tell me in this room how that is going to improve our health care system, how it is going to improve access to those who need health care, and how it is going to decrease the cost, I welcome the explanation, but I fear for the American people that this Affordable Care Act is going to dramatically affect their access to health care. It is going to dramatically affect the cost of health care. It is going to put us

into a single payer system which I believe was the ultimate goal of the Affordable Care Act.

This does nothing, nothing, to improve the free market. Let the free market decide what system works best, not the Federal Government. We are in trouble when we sit here and we have a discussion that this is the best way to go for the American people, this is the best we can do to make sure the American people have health care coverage.

I see my time has run out.

Mr. Everson, if you could comment just briefly, we have had unemployment at over 8 percent for the last 42 months. How is this going to impact our businesses in this Nation?

Mr. EVERSON. Well, in terms of the health care piece is your question? I do think that the difficult economic circumstances make the challenges that the advocate has spoken to of the constant updating of the information an even more daunting task as we go forward.

The interactions that you have spoken about that are necessary with the Service, and then the complexity, the confusion of the fact that the person is going to be going in and seeing people in the exchange or talking to the exchange and then being told, well, the IRS says you are not eligible. The IRS says you already have this or that. That is all going to converge in a situation where a lot of people, as you indicate, are already under stress because of difficult economic circumstances, or maybe they don't have a job. So I think that the circumstances of the Country right now make it inherently more difficult.

Ms. BUERKLE. Thank you, Mr. Chairman. I yield back.

Chairman ISSA. I thank the gentlelady. The gentlelady's time has expired.

We now go to the gentlelady from New York, who has been patiently waiting. Ms. Maloney?

Ms. MALONEY. Thank you, Mr. Chairman and Mr. Ranking Member, my colleagues, and all of the panelists.

Mr. Cannon, I understand that your reading of the Affordable Care Act is that it does not permit the IRS to provide premium tax cuts or tax credits to individuals who participate in health insurance exchanges administered by the Federal Government. In fact, I believe you called this illegal. Is that correct?

Mr. CANNON. That is correct.

Ms. MALONEY. Well, the Congressional Research Service has come out with a report on this, their own legal analysis, and they have examined this issue, and it did not come to the same conclusion. And, according to the report, which I would like unanimous consent to place in the record, according to the report it says—

Chairman ISSA. Without objection, so ordered.

Ms. MALONEY. Thank you so much.

It says on page eight, "The IRS rule appears to be an exercise of the authority delegated to the agency to implement Section 36(b), which includes the authority to provide refundable tax credits for taxpayers enrolled in a health insurance exchange." Have you read this report or have you seen this report?

Mr. CANNON. I am not familiar with that at all. On what date was that released, may I ask?

Ms. MALONEY. This says July 23rd.

Mr. CANNON. I will have to review that.

Ms. MALONEY. Okay. Great. Or we can get you a copy.

Mr. CANNON. I can comment on that claim.

Ms. MALONEY. But first I would like to read other portions of it, too.

The CRS also reports. It says thus: If a reviewing court “determines that there is ambiguity surrounding the issue of whether premium credits are available in Federal exchanges, the regulations issued under Section 36(b), the regulations will very likely be considered a reasonable agency interpretation of the statute and accorded deference by the court.”

Now I would like to turn to Professor Jost, if I could. Mr. Jost, you believe Congress provided the IRS authority to provide premium tax credits to individuals who participate in the Federal exchange?

Mr. JOST. That is correct.

Ms. MALONEY. And why did you come to this conclusion?

Mr. JOST. Well, again, because of the definitional sections of the statute and the way those work together, because of the structure of the statute, and because of the legislative history of the statute in which Congress, Senators, repeatedly said that tax credits would be available in all States.

Ms. MALONEY. Well, do you agree with the interpretation that I just read from the Congressional Research Service?

Mr. JOST. Yes, I do.

Ms. MALONEY. And, Mr. Jost, do you also agree with CRS that it is very likely that a court would defer to the IRS's interpretation of the statute?

Mr. JOST. That is correct.

Ms. MALONEY. And on the substance, why was it important for Congress to give the IRS this authority?

Mr. JOST. Because Section 36(b) is, as has been said a number of times, a complicated provision that requires interpretation and requires application, and the IRS has done an admirable job of putting out regulations with lots of examples in them to help people understand how this section is going to work.

Ms. MALONEY. Well thank you. I think you gave a clear indication why this is important and why it matters.

I yield back the balance of my time.

Chairman ISSA. I thank the gentlelady.

We now go to the gentleman from South Carolina, Mr. Gowdy. And I would ask the gentleman would he yield me ten seconds for a question.

Mr. GOWDY. I would yield whatever time the Chairman wants.

Chairman ISSA. Thank you.

Mr. Cannon, do you know of any Member of Congress, either side of the aisle, who said that Federal exchanges would have subsidies prior to the passage?

Mr. CANNON. Mr. Chairman, my staff and I did a pretty extensive search of the Congressional Record, including markups and Committee action, on this statute. We found only two mentions in the Congressional Record of what would happen if States did not create a health insurance exchange on their own. The first was the

chairman of the Senate Finance Committee said that tax credits are conditioned upon States establishing their own exchanges, so that affirmed——

Chairman ISSA. Barney Frank?

Mr. CANNON. No, I'm sorry, the chairman of the Senate Finance Committee, Max Baucus, who is the lead author of this law. So that confirms the clear meaning of the statute.

The only other mention was in the House during House consideration of the Patient Protection and Affordable Care Act by Congressman Michael Burgess. He said, What happens if the States don't create an exchange? Well, a Federal exchange will impose a public option. It made no mention of tax credits. Those are the only two we have found.

And Professor Jost and the IRS have not cited anything from the Congressional Record or the legislative history other than the idea that all States would be establishing their own exchanges. There is nothing that anyone else has offered that suggests that if a State does not establish an exchange that tax credits would be available in Federal exchanges.

Chairman ISSA. Thank you. Clearly, the GSA had a mind-reader at its convention. Perhaps the IRS does, too.

I thank the gentleman for yielding.

Mr. GOWDY. Yes, sir. Speaking of mind-readers, I was going to ask you, Mr. Cannon, a similar series of questions. It appears the professor is relying on the definitional section, and without putting everyone in the audience to sleep with rules of statutory construction, the last statute takes precedence over a previously passed one, all provisions must be read in harmony if they can, all the other stuff that made us very anxious to get out of law school. Why is he wrong?

Mr. CANNON. The professor makes the claim that the statute treats State and Federal exchanges equivalently. It does not. It refers to exchanges under Section 1311 as, as I quoted before, an exchange shall be a governmental agency or a nonprofit entity that is established by a State. So that is clear that they are not talking about an exchange established by the Federal Government.

The section authorizing tax credits likewise is clear. It says those tax credits are available only through "an exchange established by the State under Section 1311." Senator Baucus' original bill had language similar to what Professor Jost cites. It says if a State doesn't establish an exchange the Secretary shall "establish and operate the exchanges within the State," and Senator Baucus confirmed that tax credits, under that language, would be available only in States that establish their own exchange.

Furthermore, the statute, itself, does not address, the information reporting requirement that Professor Jost cites in his other argument refers to Section 1311 and 1321 exchanges separately. If every time the Federal Government referred to a Section 1321, if they were equivalent, there would be no need to refer to them separately.

And the Finance Committee bill, which is what became the final law, was different from the bill that was reported by the Senate Health Committee and the bill that was reported by the House in this very important way: both the Health Committee bill and the

House Committee bill had explicit language saying that State and Federal exchanges are equivalent. They drew explicit equivalents between exchanges created by States and exchanges created by the Federal Government. There is no such language in here. The definitional section that Professor Jost mentions does not establish that equivalent.

Mr. GOWDY. Mr. Everson, what new citizen information will be available to the IRS that is not currently available to them?

Mr. EVERSON. I think, sir, that the statute contemplates getting into any number of areas that are non-financial. It is true, as has been already pointed out, it is not medical information, and that is important, but you are going to be asking businesses to report on their plans and details of their plans so that the Service can determine or it can be determined whether they qualify as meeting needs under the statute.

And then you are going to have individuals, who will, as was indicated earlier, they are going to have to constantly update information about the status of employment and whether they have coverage or not. I think it can't be said enough that this need for updating and the timeliness is a very real change for taxpayers that is important, in addition to the new areas beyond purely financial information that you as a taxpayer are used to already providing.

Mr. GOWDY. Well, back in the good old days we used to have to get a court order just to get a tax return from somebody we were about to indict. What level of independence disclosure confidentiality will exist with this new information?

Mr. EVERSON. Well, I think that is something that the Service is best capable of answering. The Service historically provides great importance to the protection of taxpayer information. My concern is that there are already real protocols that exist, through working with the State taxing authority. I am from Indiana, and working with the revenue department there, or with major cities to share that information. Everybody is used to doing that.

These exchanges are going to be in the process of being stood up over a period of time. They are going to have enough they are dealing with, and yet they are going to be charged with protecting this information, as well.

You get a lot of problems with disgorging of taxpayer information or information generally. I think there is not a week that goes by where a credit card company or a business doesn't talk about hundreds of thousands of records being just spat out, and you are introducing a lot of new players here. So while there may be protocols, getting that working is going to be very challenging, and I would say fraught with problems.

The last thing I would say on this is I worry about the WikiLeaks parallel where you get not an error of the system but an individual who has lots of records and says, I don't like this law or I don't like elements of this, or so-and-so companies didn't provide what had to happen, and individuals do the wrong thing.

There is a lot of risk here, sir.

Mr. GOWDY. Thank you, Mr. Chairman.

Chairman ISSA. I thank the gentleman.

I would ask unanimous consent pursuant to the gentlelady from New York's entering into the record the Congressional Research study of just a few days ago.

The Ways and Means has forwarded a specific line in answer. "Applying the plain meaning rule to Section 36(b), it is possible that the court could read the phrase 'an exchange established by the State under 1311 of ACA' as being clear to not include an exchange established by the Federal Government." I just wanted to make sure we made it clear that was actually the verbatim of that report.

With that I recognize the gentleman from Virginia, Mr. Connolly.

Mr. CONNOLLY. Thank you, Mr. Chairman, and thanks to our panelists for being here.

Mr. Everson, in your testimony did I understand you to say that your concern is that the involvement of IRS in a major non-tax administration initiative has the potential to erode the independence of the IRS; is that correct?

Mr. EVERSON. That is absolutely true, sir.

Mr. CONNOLLY. Ms. Olson, do you share that concern?

Ms. OLSON. I think that the IRS needs to not be viewed as a political or politicized agency.

Mr. CONNOLLY. Does the assignment, however, here from the ACA, in your opinion, compromise or potentially compromise the independence of the IRS as indicated by Mr. Everson?

Ms. OLSON. I think the IRS will conduct itself in a way that it will not be compromised.

Mr. CONNOLLY. The IRS currently or recently has had, for example, assignments like the economic stimulus payments, the earned income tax credit, the first-time homebuyers tax credit, and the making work pay credit; is that correct?

Ms. OLSON. Yes.

Mr. CONNOLLY. Did the administration of any of those compromise the independence of the IRS?

Ms. OLSON. The IRS implemented the law as it understood it.

Mr. CONNOLLY. Did it compromise the independence of the IRS?

Ms. OLSON. In my opinion, no.

Mr. CONNOLLY. Mr. Everson, in your opinion did they compromise the independence of the IRS?

Mr. EVERSON. I believe that the items you are citing are pretty well within the bailiwick of traditional tax matters for the Service. What I think you have here is the potential that comes from a major Administration initiative. Again, I am making this context outside of politics and I am not making any substantive allegations. I am talking about potential systemic risk.

Mr. CONNOLLY. I understand.

Mr. EVERSON. So I have not seen it, but I think that this is quantifiably different than anything the Service has done.

Mr. CONNOLLY. Mr. Everson, unfortunately I only have five minutes, so bear with me here.

Mr. EVERSON. Okay. Go ahead.

Mr. CONNOLLY. Okay. Thank you. But let me ask this: in light of the Supreme Court ruling, Chief Justice Roberts' ruling and that horrible word tax, doesn't that, in fact, add more weight to the role of the IRS, not less?

Mr. EVERSON. No doubt it does. That is right.

Mr. CONNOLLY. If I can, Mr. Everson.

Mr. EVERSON. Yes.

Mr. CONNOLLY. But it seems to me to put to bed a little bit the concern you have, maybe not you personally, about independence of IRS when the Chief Justice of the Supreme Court and a majority ruling of the Supreme Court says otherwise, that it most certainly is within the purview; in fact the responsibility of the IRS, by virtue of his decision of what constituted the Constitutionality of the act.

Mr. EVERSON. Well, clearly that has justified the operation of the individual mandate, yes.

Mr. CONNOLLY. Thank you. I'm sorry.

Mr. EVERSON. That is okay. Go ahead.

Mr. CONNOLLY. I have a limited period of time here.

Mr. EVERSON. We obviously disagree.

Mr. CONNOLLY. I understand, but we have a Supreme Court ruling.

Mr. EVERSON. Of course.

Mr. CONNOLLY. And God knoweth why, but they didn't invoke the Commerce Clause; they invoked something else. So there we are.

Professor Jost, are you familiar with RomneyCare in Massachusetts?

Mr. JOST. I am familiar with the Massachusetts reforms, yes.

Mr. CONNOLLY. Well, it seems to me if we are going to call the ACA ObamaCare, we will call health care reform in Massachusetts—

Mr. JOST. I don't, so I am trying to be even-handed.

Mr. CONNOLLY. I understand. I am trying to be even-handed, too.

What is the role of the Massachusetts Department of Taxation, which is the analog in Massachusetts? I happen to come from Massachusetts originally. What is the role of the Massachusetts Department of Taxation in the administration of this particular set of issues in RomneyCare?

Mr. JOST. I believe there are premium tax credits in Massachusetts.

Mr. CONNOLLY. Really? And when fines or penalties are imposed, as they are under the law signed into law by the Governor of Massachusetts at the time, Mitt Romney, how is that administered?

Mr. JOST. Through the tax system.

Mr. CONNOLLY. Through the tax system. Is it not virtually identical to the system Ms. Olson described that will pertain to the ACA?

Mr. JOST. The ACA was modeled on the Massachusetts health care reforms.

Mr. CONNOLLY. So, for example, as Ms. Olson was testifying a little bit earlier, most people have a refund and you would net out the refund if you owed that fee; is that correct?

Mr. JOST. I believe so.

Mr. CONNOLLY. And is that not exactly how Massachusetts works?

Mr. JOST. I believe so.

Mr. CONNOLLY. Ms. Olson, is that your understanding, as well?

Ms. OLSON. I am not an expert on Massachusetts. I can only speak about the Federal provision.

Mr. CONNOLLY. I see. Final point, maybe Ms. Olson, to you, there is a return for every dollar we invest in the IRS; is that not correct?

Ms. OLSON. Yes.

Mr. CONNOLLY. And is it my understanding for every dollar IRS got it produced \$200 in revenue?

Mr. CONNOLLY. That is the ratio of what we collect to our appropriated—

Mr. CONNOLLY. So, given our obsessive concern about the fiscal situation and the National debt, Congress has, in fact, increased IRS's budget, given that ratio, so we can collect that which is owed; is that not correct?

Ms. OLSON. You are still working on our appropriation this year.

Mr. CONNOLLY. What has happened in the last three or four years?

Ms. OLSON. Actually, last year our budget was decreased.

Mr. CONNOLLY. Decreased?

Ms. OLSON. Yes.

Mr. CONNOLLY. And what is the total amount of revenue owed the Government, not new taxes, that is left on the table every year because of lack of collection?

Ms. OLSON. It is about \$359 billion or something in that range.

Mr. CONNOLLY. So \$359 billion a year. Now, if I multiply that times ten, that would be over \$3.5 trillion; is that correct? And your understanding of the value of the sequester we are so concerned about, we are not going to cancel our five-week recess to do anything about, is \$1.2 trillion; is that not correct?

Ms. OLSON. I'm sorry. I am not following your question.

Mr. CONNOLLY. The value of the sequester we are worried about is \$1.2 trillion; is that not correct?

Ms. OLSON. That is my understanding.

Mr. CONNOLLY. And the amount you are talking about over that same period of time would be three times that.

I thank the Chair.

Ms. BUERKLE. [Presiding]. Thank you.

The Chair recognizes the gentleman from North Carolina, Mr. McHenry.

Mr. MCHENRY. Thank you, Madam Chair.

Look, Americans know that the tax code is complex. That is obvious to even those that don't pay taxes. I think it is one of the self-evident truths the American people have. I have run into an issue in western North Carolina dealing with small fire departments. I have got about six to eight of them that, based on a provision of the law and how the IRS chose to implement it, means that these volunteer fire departments that are quasi-governmental non-profits, they receive taxpayer funds and they actually have tax collection areas. We have this whole thing. And so my office has had to be engaged in making sure these non-profits still get to maintain their non-profit status based on how the IRS has implemented it.

And so there is a lot of grief the American people have with the IRS and we have got public safety at risk based on how the IRS has chosen to implement a law.

And so I want to say, Ms. Olson, your office, the National Taxpayer Advocate Office in Greensboro has been enormously helpful to us in going through this whole process and trying to be truly a taxpayer advocate for these volunteer fire departments in my District, and I want to thank you for that. This has been enormously frustrating and confusing, but I certainly appreciate the work that you do and the work that your staff does. Thank you.

Ms. OLSON. Thank you, sir. I am personally very familiar with that issue, and it is on my radar screen and we are working on this.

Mr. MCHENRY. Thank you. I certainly appreciate it, and I hope that the commissioner hears this, as well, and that you have some compliance on behalf of taxpayers, the IRS actually has some compliance.

To that end, and the reason why I bring this up is because it is about the confusing and complex nature of the tax code. And that is frustrating as it now stands, as it now stands. That is before we even talk about ObamaCare, as my colleagues on the other side of the aisle like to call the affordable health care or whatever else, any way they want to call it, but the point is if you look at how the Internal Revenue Service is going to have to implement ObamaCare and portions of ObamaCare, Mr. Everson, you have testified well on this.

So in your testimony you expressed doubt as to whether the statutory scheme as enacted into law is even workable mechanically. What do you mean by that? Explain. The IRS can, you know, has a complex enough code. Are you saying that this is even beyond?

Mr. EVERSON. I am suggesting that there are so many parts and there are so many players that we cannot, by any means, be sure that this is going to work. That is not getting at the policy objections that some have raised, it is just simply as a matter of management. That is particularly the case because of the fact that there are different levels of government. You have got different agencies of Government in the Federal level, and then you have got States and you have got these quasi-State entities, these exchanges.

All of these are players, plus private parties, companies and individuals. All of this interacting together across these multiple provisions I think really is an extraordinarily daunting task from a managerial point of view. That is what I am getting at, sir.

Mr. MCHENRY. Okay. So thus, you know, if they have more folks collecting taxes and the tax code is more engaged in people's daily lives and health care decisions?

Mr. EVERSON. Well, what I am saying here is that the other piece, whether you get this done or not, the other facet of my testimony is that I am concerned that by doing this, by assigning these health care responsibilities to the Service, which are contentious. They are certainly, as we know from this hearing, contentious politically, but they are going to be contentious for individuals because, as was indicated by the Chair, these are the intensely personal issues. That is the word you used. And I agree with that.

You are adding into the interaction of the citizenry with the IRS another highly-charged element of a conversation, if you will, and

that can't help but impact how they feel about tax collection, as well.

Mr. MCHENRY. Ms. Olson, to this point, with implementation and your preparations for implementation of ObamaCare, how daunting and how difficult is this task going to be for the average American to be in compliance with this? You say that with the mid-year they are going to have to update if they change jobs, as they receive more income rather than less, or less income rather than more? For your planning purposes, how complex is this going to be and how much of a challenge is this going to be?

Ms. OLSON. Well, it is going to be a challenge for individuals and the IRS and for the exchanges, and commissioner Everson is correct about all the moving parts. The taxpayers' ongoing responsibility to update is going to be not with the IRS but with the exchanges, where the taxpayer is going to interact with the IRS at the end of the year with the return filing, and that is where we do a reconciliation of what they got during the year and then what they actually were entitled to based on what really happened with their income and their family structure during the year, and there is a possibility of a gap between that, and that will come as a rude surprise to some taxpayers.

That is why I have emphasized that we have to really educate taxpayers about their responsibility to talk to the exchanges. My concern is similar to Mr. Everson's in that taxpayers are going to look to the IRS, partly because we are talking about the IRS all the time about this, and call the IRS and want to give updates of information to the IRS, and they will be confused. Where do they go? And will they get to the right place? And will the IRS be helpful in telling them, here is where you need to go?

I have said IRS employees have to have a Rolodex of where to send these individuals so they can get to the right place.

Mr. MCHENRY. Oh, Lord. With that I yield back.

Ms. BUERKLE. Thank you.

The Chair now recognizes the gentleman from Arizona, Dr. Gosar.

Dr. GOSAR. Thank you, Madam Chair.

Ms. Olson, you made an interesting finding. Oh, by the way, I am a health care provider. I am a dentist. Okay? So I know something about this. You talked about changing behavior. Is that pretty easy, changing behavior?

Ms. OLSON. No.

Dr. GOSAR. How would you feel about that, Mr. Everson?

Mr. EVERSON. I'm almost 58. It is tougher every year.

Dr. GOSAR. I understand that. Ms. Olson, are you familiar with the Advanced Federal Child Tax Credit?

Ms. OLSON. Yes.

Dr. GOSAR. What were their instructions to the American people. Please do not call the IRS, right?

Ms. OLSON. Yes. That was in 2001.

Dr. GOSAR. How many calls did you get?

Ms. OLSON. In one day we got about, it was our first million call day, and they called asking do we really not need to call you.

Dr. GOSAR. So, I mean, when you are talking about customer service associated with this, this is much more complex?

Ms. OLSON. Yes.

Dr. GOSAR. Would you say exponentially?

Ms. OLSON. Yes. It goes to my earlier point: it is not that we have new powers or new duties, it is the scope.

Dr. GOSAR. I understand.

Ms. OLSON. It is the amount of work.

Dr. GOSAR. So how many customer service people are you planning on hiring?

Ms. OLSON. Well, I am not planning on hiring people until I know what my budget is. I think that is a question for the Commissioner. I have heard that we will be focusing on about 800 FTE that will be partly IT and majority working on the customer service side.

Dr. GOSAR. Mr. Everson, tell me, given the quantum leap that we are doing here for customer service, in your estimations what kind of customer service detail would we need to handle this?

Mr. EVERSON. I haven't studied it in such detail that I would be able to give you a number. I mean, the Service is more than capable of having that conversation. But you are really talking, just as the Advocate has said, as Nina has said, you have got a whole new area of responsibilities, you have got potential for whole new conversations.

In the Act, frankly, it extends well beyond that. Small businesses, we work at AlliantGroup where I am now, we work with small and mid-sized businesses. They are flummoxed by the statute and all the different obligations that they have. So there are lots of different parties that are going to be impacted by these changing standards, including maybe your dentist shop. I don't know.

Dr. GOSAR. Absolutely. We have kind of kept the Federal Government away as best we can. But that is my whole point is this is an ongoing dialogue that should be going on the whole year, not just at reconciliation, because it is compensatory backlog. So it is customer service intensive, would you say? So 800 FTEs ain't going to work.

Ms. OLSON. Well, that is the spec'ing out, but I have not seen the details behind that.

Dr. GOSAR. Going back to changing behaviors, when you are sharing all this information, you know, and exponentially enlarging the pool of people accessing your personal information, boy, I tell you what, you had better have customer service. And, if I am not mistaken, you are not really known for customer service, right?

Ms. OLSON. We need to improve our taxpayer service.

Dr. GOSAR. So let me ask you this: what is your average wait for a person for customer service?

Ms. OLSON. I think this year it was about 12 minutes on the main phone line.

Dr. GOSAR. For an expedited form, right?

Ms. OLSON. Yes.

Dr. GOSAR. How much longer when we have questions?

Ms. OLSON. I don't know the answer to that. On some lines these have been—

Dr. GOSAR. Hours? Days?

Ms. OLSON.—hours. Yes.

Dr. GOSAR. Days. I'm just saying on the phone just trying to get somebody that is qualified to answer.

Ms. OLSON. Yes.

Dr. GOSAR. And this is much more, as we have heard the witnesses talk about, exponentially just growing in size.

Mr. EVERSON, I am really perplexed by the safety. I know I couldn't find at least a sizeable leak from the IRS in personal information.

Mr. EVERSON. Right. It has got a very good record.

Ms. OLSON. It does.

Mr. EVERSON. It is a real strong point of the Service.

Dr. GOSAR. But the one problem that we have got is we are going out beyond that because we are going to be sharing this information all over the place, and we are also subjugating individuals to insurance companies, are we not?

Mr. EVERSON. There is a tie-in into the insurance companies. I am not sure how that will work on the exchange of what they will have in terms of the taxpayer information, but clearly you are exactly right. When you get to the exchanges or you get to the other States, you are going to have a whole new set of players that are dealing with not just the traditional information but even more information.

Dr. GOSAR. So how do we guarantee that that is, and you alluded to it. It is sort of like my gentleman friend from South Carolina, you know, this is the potential to share very personalized, like the gentlelady up here said, for sharing personal information.

Mr. EVERSON. There are no guarantees in this area, sir, and it just is a very significant area of continuing focus by the Service. I would tell you any business in America now that deals with this kind of information, it is something that everybody worries about, but this does increase risk. That is all I am saying.

Dr. GOSAR. One last question. Do you think the health care is individualized and should be personalized, patient friendly? Personally, your point of view?

Mr. EVERSON. I am not going to answer a policy question on health care. I have not got a dog in that fight today. How is that?

Dr. GOSAR. You do, because your health is yours today and you own it, right?

Mr. EVERSON. Yes.

Dr. GOSAR. How about you, Ms. Olson?

Ms. OLSON. I am not going to answer that question.

Dr. GOSAR. You don't own your health today?

Ms. OLSON. I do own my health today. I just went to my dentist last week.

Dr. GOSAR. God love you, and you are smiling. How about you, Mr. Jost?

Mr. JOST. I believe that my health care is personal, and I believe that the Affordable Care Act protects it.

Dr. GOSAR. Mr. Cannon, how do you feel about that?

Mr. CANNON. Health care is, of course, an intensely personal issue. There is a difference of opinion among obviously supporters and opponents of this law because, just like other opponents of this law, I think it is going to make access to health care less secure, not more.

Dr. GOSAR. Thank you very much.

Mr. CANNON. And cause more people to fall through the cracks.

Mr. EVERSON. Maybe I misunderstood your question, sir. If you are saying do I think information about my health care is personal and shouldn't be shared, yes, I agree with that.

Dr. GOSAR. Thank you very much.

Ms. BUERKLE. Thank you. The Chair now recognizes the gentleman from Idaho, Mr. Labrador.

Mr. LABRADOR. Thank you, Madam Chair.

Mr. Cannon, my State right now, Idaho, is going through a huge debate about whether we should accept the health insurance exchange, should we do a Federal exchange or do a State exchange, and interestingly I have made a recommendation to our governor and to our legislature that they shouldn't at this time accept a health insurance exchange as a State exchange, that they should allow it to become Federalized. So I want to have a little discussion with you about this. Have these true State exchanges that we are talking about when you are talking about State exchanges under ObamaCare?

Mr. CANNON. No. The statute requires that every State-created exchange, in order to be compliant with ObamaCare, that it has to get approval from the Secretary, and the statute gives the Secretary the authority to heap pretty much whatever sorts of regulations the Secretary wants onto these State-created exchanges.

So it really is a myth, the idea that States would be able to retain some sovereignty, retain some control over their health insurance markets if they create their own exchanges, because whatever the Secretary would be able to impose on a State through an exchange that the Federal Government created, the Secretary could also impose on a State-created exchange through regulation.

Mr. LABRADOR. Well, you and I probably have very similar philosophies about the 10th Amendment and States' rights. It seems odd that somebody from the Cato Institute and a conservative Republican from Idaho are asking a State to forego the State exchange and actually allow for the Federal exchange. Could you explain?

Mr. CANNON. Well, it is a little bit ironic, but what you want is a Federally-run health insurance exchange in your State, which is really just a Government agency controlling the private health insurance market. If what you want is the Federal Government to control your State, then the best thing you can do is establish an exchange because the Federal Government will control it.

If a State does not establish an exchange there might not be an exchange at all, because, as we all know, there is no funding in the act for the Federal Government to create these exchanges, and it is not likely that Congress is going to approve that funding any time soon, so this is a real problem for the Administration. They are having to take money away from other things that Congress appropriated money for. I would like to see an investigation into that, frankly.

But the choice is not between a State-controlled exchange and a Federally-controlled exchange; it is between a Federally-controlled and maybe none.

Mr. LABRADOR. Okay. If a State would have set up its own exchange independent of ObamaCare, would the IRS penalties apply?

Mr. CANNON. The IRS penalties against individuals who do not comply with the individual mandate would apply?

Mr. LABRADOR. Right.

Mr. CANNON. Penalties under the statute, the penalties against employers, the \$2,000 per worker tax that the Patient Protection and Affordable Care Act imposes on employers in States that create their own exchanges would not apply in a State that does not create its own exchanges. So Utah, for example, could avoid that very large tax on employers by not creating an exchange, and what this IRS rule does is, it first deprives Utah of that choice, and then imposes that tax illegally on those employers.

Mr. LABRADOR. Okay. But if a State sets up an exchange under ObamaCare, it is subject to the IRS penalties, right?

Mr. CANNON. It is subjecting its employers to the employer mandate, which is a \$2,000 per employee tax.

Mr. LABRADOR. Okay. So when you are making the decision about whether you are going to set up a state exchange, you have to think about those taxation issues for your employers in your State?

Mr. CANNON. As well as what employers in neighboring States, I'm sorry, the government's neighboring States are doing, because if you are in Utah and your neighbors all decide not to create a health insurance exchange but you create one, you will be imposing a tax on your employers that your neighbors are not, and they may want to leave your State for other States.

Mr. LABRADOR. Okay. Isn't it true that under the actual text of the law that if a State does not set up its own ObamaCare exchange and the Federal Government steps in and sets up its own exchange that the IRS penalty does not apply?

Mr. CANNON. The employer mandate, that is correct, because what triggers that \$2,000 tax on employers is when one of that employer's workers receives a tax credit through an exchange. Again, under the statute if there are no State-created exchanges there can be no tax credits to trigger that penalty against employers.

Mr. LABRADOR. And in the concept of federalism, the concept of having the State create something that it can manage, is it truly a State-managed exchange if you are doing it under the rules of ObamaCare?

Mr. CANNON. Absolutely not, and for the reasons I just mentioned as well as the fact that there will be hundreds of billions of dollars flowing through these exchanges from the Federal Government, so the Federal Government is going to be controlling all of that money. The Golden Rule applies here.

Mr. LABRADOR. And I just want to be clear. So when you say that, you mean that since they are controlling the money they are going to be telling the State what rules apply for that State exchange, and what compliance, correct?

Mr. CANNON. That is correct. For example, Utah's exchange would not qualify under—

Mr. LABRADOR. Under ObamaCare. Correct. Even though they did it before ObamaCare, correct?

Mr. CANNON. Correct.

Mr. LABRADOR. So, in essence, all the State exchange is is another Federal agency?

Mr. CANNON. For which the States will have to pay, because if a State opts to create its own exchange it is responsible for the operating costs of that exchange. The estimates have been \$10 million to \$100 million per year.

Mr. LABRADOR. All right. Thank you very much.

Mr. CANNON. Thank you.

Ms. BUERKLE. I thank the gentleman.

I now recognize the gentleman from Pennsylvania, Mr. Kelly.

Mr. KELLY. I thank the Chairwoman, and I thank all of you for being here today. This is critical.

I had a conversation yesterday, and then also today, with Stephanie McCafferty, an automobile dealer who still owns the business. My son runs it. We did build it by ourselves, by the way. We have had this continuing conversation trying to determine exactly what this new Patient Protection Affordable Care Act actually does to us, and I have got to tell you, even after sitting down with the CRS for an hour everybody still scratches their head and says, You know what? We don't know. We just don't know.

So, Mr. Everson, let me ask you this: is it true that the IRS will have to collect ObamaCare's employer mandate penalty?

Mr. EVERSON. Yes, sir. There will be an obligation upon the Service, like in many other areas, to make that assessment based on the information that is provided.

Mr. KELLY. And that mandate penalty amounts to a \$2,000 or \$3,000 penalty per worker?

Mr. EVERSON. I believe that is the case. I am not an expert in the exact figures.

Mr. KELLY. I haven't found anybody that is an expert in any of this. You are not offending me by answering that way.

Mr. EVERSON. Yes.

Mr. KELLY. It is a very difficult thing. Also, since the ObamaCare mandate penalty is assessable in the same manner as other employment tax penalties, is it true that the IRS does not have to offer the employer an opportunity to review and contest the determination prior to assessing the penalty?

Mr. EVERSON. Well, I would say, sir, that is a question for the Service to address. It is an interpretation of the law and they have got to write the appropriate regs. I would expect that the Service will be very careful in laying all this out and want to get, because of the problems we have been talking about all morning, the nature of small businesses, lack of sophistication and understanding of the tax code, they are going to want to get this right, whatever they do, so they are going to have to work very hard. They are going to have to work very hard to do it, and then that is one piece of it.

My other concern is then whether the folks in the businesses will understand it, actually.

Mr. KELLY. In our business we buy and sell cars and we service cars and trucks and that is what we do.

Mr. EVERSON. Yes.

Mr. KELLY. Now, in addition to that, the greatest amount of time we spend now in the back office is not dealing with the services we

offer our customers, it is trying to be in compliance with the Government that continues.

I have got to tell you, when I am opening the mail if it says it is from the Federal Government or the State government or the local government I say, What are they going to take from me now, or, How are they going to regulate me and make it harder for me to get through this business?

Is there any appeals that exist, that come into play—and it happens after the collection begins, right, so if IRS comes in, they sit down, they talk with me and say, By the way, it starts now, it starts today.

Mr. EVERSON. The Service has very clear procedures on appeal rights, and even before things happen you can raise matters up with supervisors, but I do think that there are going to be, this is another area where there is going to be more confusion. Some of these, as the taxpayer advocate has indicated, the provisions are different in certain standards as to what actions on an enforcement side the Service can take. I have written in my testimony I am concerned about that. Any time you introduce variability into a huge operation it is harder to run.

So I think that these are all issues that are going to be tough to deal with.

Mr. KELLY. And really I am on board with you. It is truly the uncertainty of what this law is asking us to do that creates this. I am talking now about job traders. You have got to stay on the sidelines because you are not sure that your actions are going to cause a problem for you. And I have been through tax audits, and I have got to tell you the thing that strikes fear into the hearts of most Americans is that the IRS is coming in to do an audit.

Again, you say, my gosh, I know we did everything we thought we were supposed to do, but I guarantee you that small business owners who do not have, as you say, a level of sophistication, I mean, who does have the level of sophistication? It is certainly, even this panel with its vast knowledge and its experience, it is like I know something about it but I don't know everything about it. And then we go to the job creators, the small business people and say, You know what? The ball is in your court right now. How do you stand up and do that?

So let me ask you, Ms. Olson, how long does a business have to pay penalties assessed by the IRS under the employee mandate?

Ms. OLSON. There is a ten-year collection statute. And I do want to say about the penalty, the small business penalty, that it applies to employers with over 50 employees, so there already is carved out by the law the very small.

I think Commissioner Everson is correct that we have got to really work on this with the regulation and the appeals procedures, and if there is an ability to get reasonable cause, abatement of penalties, the things that we normally do with penalties, those are very important issues.

Mr. KELLY. And, again, if I understood, you said the penalties are very small?

Ms. OLSON. No. The have exempted the very small businesses from the penalties.

Mr. KELLY. Under 50?

Ms. OLSON. Under 50 employees.

Mr. KELLY. Okay. Well, a lot of my friends have more than 50 people, so it applies to an awful lot of them.

Ms. OLSON. Right.

Mr. KELLY. So if a business reports an IRS error, how long will it take the IRS to fully investigate? Any ideas at all?

Ms. OLSON. The IRS has three years from the filing of a return, in general, to investigate.

Mr. KELLY. All right. So I would just suggest, and I offer this only as a small businessperson who has lived in the private sector for his whole life, gosh, you are making it hard for us. You are making it so hard for us. I would ask each of you, who signs your paycheck?

Mr. EVERSON. Sir, I would tell you, you have made it hard for taxpayers, not the IRS. Let's get this right. You wrote this law, the Congress did.

Mr. KELLY. You know what, Mr. Everson, I just got here. I have only been here for 19 months. No, I didn't write it. In fact, nobody even read it before they passed it, so let's make sure we are very clear in what happened, okay?

Mr. EVERSON. Okay.

Mr. KELLY. And even the people that are sitting here on this panel today cannot tell us specifically what the penalties are going to be and how much it is going to cost small job creators like myself. So we can tap dance around this and we can pretend that it didn't happen.

I am going to show you right now this Government is crushing job creators and turning away and saying, you know what? The problem with you folks, you just don't have the level of sophistication to understand this entire law. As a matter of fact, neither do we, but we do have the ability to come in here and tax you. We have the ability to come in here and shut you down. We have the ability to hold you accountable for a law that not even we understand. So how do you like that, Mr. Car Dealer? How do you like that, Mr. Carpenter? How do you like that, Mr. Manufacturer? How do you like that, Mr. Miner and Steelworker?

Come on. Let's be honest with each other. This is absolutely astounding that we would have to have this conversation. You are paid by the same people that I am paid by, and that is the taxpayers of this great Country, and we have made it so hard for those folks to live the way that the Founders designed this place.

I am going to yield back my time because I am way over time, but I will never stop fighting for the small job creators that are out there and the small business people who have nobody else to turn to. I have sat through it, and I mean that sincerely. There is nothing that strikes fear in the hearts of people that own businesses than the fact that the IRS is showing up. Boy, I tell you what, you try to circle the wagons and get all your information together.

When it comes to the point that I have to worry more about not competition down the street but I have to worry about my own Government holding me back, there is something wrong.

Chairman ISSA. [Presiding]. I thank the gentleman for yielding back.

I thank our panel for the generosity of all of your counsel.

Mr. Everson, I appreciate your recognition and, to be honest, your seeing both sides. I agree with you on a personal basis that Congress deserves the blame, noting that you are no longer on the Federal payroll.

Ms. Olson, I would like to thank you personally for the fact that your various reports and counsel of some of the areas of concern were areas that we took note of here.

Professor, I thank you very much for putting out your position in a very accurate way. I appreciate your being here.

Mr. Cannon, it is always a pleasure to have Cato represented here. I think you did a great job of expressing their concerns. Ultimately, much of what we said here today will ultimately be decided outside of Congress in all likelihood.

This has been a great panel. We stand in recess. Yes, Mr. Everson?

Mr. EVERSON. I just want to thank the Chair and the Members for keeping me out of this exchange fight. I didn't get any of the questions. Thank you, sir.

Chairman ISSA. Well, Mr. Everson, as you go back and talk to small businesses you consult with, I am sure they will have questions about that for you, so you are not going to be out of the fight in the other side of your life.

Thank you again. We stand in recess until ten minutes after the second vote.

[Recess.]

Chairman ISSA. The Committee will come to order.

It is now our honor to introduce our second panel witness, The Honorable Douglas Shulman, who is the Commissioner of the IRS, a post that he has held since he was appointed under President Bush nearly five years ago.

Welcome.

Pursuant to our Committee, I would ask you to rise and take the oath and raise your right hand.

Do you solemnly swear or affirm that the testimony you are about to give will be the truth, whole truth, and nothing but the truth?

[Witness responds in the affirmative.]

Chairman ISSA. Let the record indicate the gentleman has answered in the affirmative. Please have a seat.

As I noted during the first panel, you did a great job of staying focused on what was going here from the back. You have obviously done this many times before. Since you are the only witness, we won't hold you strictly to the five minutes, but I would ask you to remember that your entire written statement is in the record.

With that, the gentleman is recognized.

STATEMENT OF DOUGLAS SHULMAN

Mr. SHULMAN. Thank you, Mr. Chairman. And thank you for having me here. Thank you, Ranking Member Cummings and other members of the Committee.

Immediately upon enactment of the Affordable Care Act, or ACA, we began our implementation efforts, which included both executing on the short-term provisions that were in the bill that were

our responsibilities, as well as putting a structure and process in place to plan for provisions with future effective dates.

The IRS moved very quickly on some of the law that became effective immediately. For example, we conducted outreach and implementation for the small business health care tax credit. The ACA, as you know, also expanded the adoption credit immediately and provided favorable tax treatment for adult children up to age 26 who are covered by their parents' insurance.

The IRS's most substantial implementation effort relates to the delivery of hundreds of billions of dollars in premium assistance tax credits that will help millions of American families afford health insurance starting in 2014.

Now, the Department of Health and Human Services is the lead agency in defining the structure and operations of health insurance exchanges, with the Treasury and the IRS defining the associated rules for how the tax credits can help subsidize coverage.

It is important to note that the credit will be paid directly to the insurance company, which is a major design feature which should help mitigate the risk of fraudulent claims.

Taxpayers will then reconcile the advance payments they receive on their tax return. If the credit is larger than the sum of the advance payments, the taxpayer will be entitled to a refund. If the credit is smaller than the sum of the advance payments, the taxpayer will owe the difference.

Now, starting in 2014 individuals who can afford health insurance coverage and are not eligible for an exemption must either purchase minimum essential coverage or make a payment with their tax return. The payment only applies to taxpayers who can afford insurance but do not purchase it.

We are already working with tax return preparers and the tax software community to give taxpayers the tools that they will need to fill out their returns in 2015. The IRS process for verifying coverage will be very similar to the one we have used for years to verify wages and withholding. The IRS will match what is reported on the tax return with the information reported by the insurers.

For the small number of taxpayers who may appear to have underpaid and were not eligible for an exemption, we will generally follow up with written correspondence.

I think it is important that I clarify one misconception. Revenue agents who are trained on much more complex tax issues do not work on resolving these kinds of issues. The law also clearly specifies that the IRS will not use levies or file notices of Federal tax liens if the taxpayers have unpaid amounts related to the individual coverage provision.

Because these and other ACA provisions are substantial and require long-term planning, we immediately established processes within our business operations and our IT operations to make sure we could implement the law smoothly.

Before closing, let me just observe that the IRS is continuing its long tradition of being a nonpartisan agency that implements the laws that Congress passes. As the Chairman mentioned, I started my tenure in 2008, and right when I walked in the door we were asked to, outside of the tax systems, figure out a way to send 100 million Americans stimulus checks which the previous Administra-

tion did as the recession started to hit. We also played a role in the Recovery Act. During the serious economic downturn we set up special programs we called Fresh Start to work with struggling taxpayers, and now we are working on the Affordable Care Act.

I believe the effort is going smoothly. I believe we have the proper plans in place. And all of this is a tribute to the dedicated professional men and women at the IRS who have devoted long careers to fair and even-handed administration of the Nation's tax laws.

Thank you. That ends my opening statement.

[Prepared statement of Mr. Shulman follows:]

**WRITTEN TESTIMONY
OF
COMMISSIONER OF INTERNAL REVENUE
DOUGLAS H. SHULMAN
BEFORE THE
HOUSE OVERSIGHT AND GOVERNMENT REFORM COMMITTEE
HEARING ON
IMPLEMENTATION OF TAX LAW CHANGES IN
THE AFFORDABLE CARE ACT
AUGUST 2, 2012**

INTRODUCTION

Chairman Issa, Ranking Member Cummings and members of the Committee, thank you for the opportunity to appear before the Committee to update you on the IRS' staged implementation of the tax law changes contained in the Affordable Care Act (ACA).

Whenever Congress passes changes to the tax law, the IRS must take the necessary steps to educate and communicate with taxpayers about the changes, update relevant forms and publications, change or reprogram its information technology systems, and implement appropriate programs to sustain high levels of compliance with the new provisions. The Affordable Care Act is no exception.

Both short-term implementation and long-term planning began immediately upon passage of the legislation. Our efforts focused on: (1) ensuring tax law changes that were retroactively or immediately effective were implemented in an expedited manner; and (2) putting structures and processes in place to begin planning for provisions with future effective dates.

EARLY IMPLEMENTATION EFFORTS

The IRS moved quickly to implement a number of tax law provisions in the ACA that immediately went into effect upon enactment. Let me discuss a few provisions that the IRS implemented immediately upon enactment of the ACA in 2010.

The IRS conducted an extensive outreach and implementation program for the Small Business Health Care Tax Credit. Shortly after the Affordable Care Act was passed, the IRS determined the necessary steps to both implement the credit and track these efforts. The IRS conducted significant outreach, communication and educational activities to inform small businesses and tax professionals about the credit.

We created a special page on our web site, IRS.gov, just for the Small Business Health Care Tax Credit. From there, taxpayers could use a step-by-step guide to see if they qualified for the credit and how to claim it. There are also links to a Question and Answer section, a special YouTube Video, legal guidance, news releases, and information flyers.

The Affordable Care Act also expanded the existing adoption tax credit. The dollar value of the Adoption Credit was not only increased from \$12,150 to \$13,170 but was also made refundable. In 2010, we issued guidance on the expanded adoption credit and updated forms and instructions so that eligible taxpayers could claim the newly expanded adoption credit on their 2010 tax returns.

Taxpayers and practitioners could also find on IRS.gov a step-by-step procedure for claiming the credit, including a link to “Instructions for Form 8839” which has a detailed list of the acceptable required documentation. The documentation required can vary depending on whether it is a domestic or foreign adoption.

This online article also spells out what happens if a taxpayer’s return claiming the credit is selected for review. For example, the taxpayer will receive a notice from the IRS explaining the steps he or she must take, such as providing certain documentation to resolve the issue.

Finally, the IRS quickly communicated with taxpayers and issued guidance relating to the ACA provision requiring group health plans and health insurance issuers that provide dependent coverage of children to continue to make such coverage available for an adult child until age 26. The ACA amended the Internal Revenue Code to give certain favorable tax treatment to this coverage for adult children. The IRS guidance explained that the statutory provision provides that health coverage provided for an employee’s children less than 27 years of age is generally tax-free to the employee, effective March 30, 2010.

PREMIUM TAX CREDITS

The IRS’ most substantial implementation effort relates to the delivery of premium assistance tax credits that will help millions of American families afford health insurance starting in 2014.

The Department of Health and Human Services (HHS) is the lead agency on defining the structure and operations of the Affordable Insurance Exchange or, “Exchanges,” with Treasury/IRS defining the associated rules for how tax credits can help subsidize the coverage available through the Exchanges.

Starting in 2014, individuals who do not have access to affordable employer-sponsored insurance or other minimum essential coverage may be eligible to receive advance premium tax credits for private insurance that they purchase through the Exchanges. HHS has published guidance on how the Exchanges will administer the advance payments of the credits. It is important to note that the advance payments of the credit will be paid directly to the insurer, and cannot be accessed directly by the taxpayer.

Taxpayers will reconcile these advance payments on their tax return. If the actual credit is larger than the sum of advance payments, the taxpayer will be entitled to a refund. If the actual credit is smaller than the sum of the advance payments, the taxpayer will owe the

difference, subject to caps for certain individuals included in the Affordable Care Act, as amended.

Separately, the Affordable Care Act provides an important role for tax return information in helping to determine eligibility for both Medicaid and premium tax credits. IRS staff has been working closely with HHS and the states on developing secure and efficient systems.

MINIMUM COVERAGE PROVISION

The Affordable Care Act also stipulates that starting in 2014 individuals who can afford health insurance coverage, and are not eligible for exemptions, must either purchase minimum essential coverage, or make a payment with their tax returns.

The individual minimum coverage provision is projected to affect only a small percentage of the total population when it comes into effect in 2014. The Congressional Budget Office and Joint Committee on Taxation estimate that approximately four million people – approximately 1 percent of the projected population – will make a payment (or, in the case of dependents, have a payment made on their behalf) in 2016. Let me be clear that the payment only applies to taxpayers who can afford insurance but do not purchase it. There are also a number of individuals who will be exempt from the individual coverage provision, such as those with income below the tax filing threshold or those whose premiums are not affordable.

Taxpayers will get a form at the end of every year from their insurer which they will use when they prepare their tax returns. It is important to note that the information that insurers provide to the IRS will show fact of insurance coverage, and will not include any personal health information.

In most cases, taxpayers will file their tax return reporting their health insurance coverage, and/or making a payment, and there will be no need for further interactions with the IRS. The IRS process for verifying coverage will be very similar to the one that the IRS has used for years to verify wages and withholding. The follow-up will generally be performed by written correspondence, and will allow taxpayers time to gather the information needed to respond, or get help in understanding the details of the provision.

In this regard, let me clear up one misconception. Generally, revenue agents – who are specially trained on more complicated aspects of the tax code – would not work on resolving these types of issues, just as they don't work on resolving mismatches between W-2s and income tax returns today. Typically, these issues are addressed and resolved through written correspondence.

The law also clearly specifies that the IRS will not use levies or file notices of federal tax lien if taxpayers have unpaid amounts related to the individual coverage provision. Moreover, taxpayers will not be criminally prosecuted for non-payment of this amount.

IMPLEMENTATION EFFORTS

Because these and other tax provisions included in the Affordable Care Act are substantial and require long-term planning, the IRS has established enterprise-wide governance and planning processes, both in its business operations as well as its information technology division. These planning efforts have had the benefit of independent reviews by both the Government Accountability Office (GAO) and the Treasury Inspector General for Tax Administration (TIGTA).

Our budget requests in recent years reflect the need to invest in information technology (IT) systems to generally update our tax systems as well as administer the premium tax credit and other tax law provisions of the ACA. Of the funding requested in our FY 2012 and FY 2013 budgets related to ACA tax law implementation, 82% and 92%, respectively, was in our Operations Support account, which funds our IT and operations investments.

CONCLUSION

Mr. Chairman, thank you again for this opportunity to testify on the IRS' planning and implementation efforts related to the tax provisions contained in the Affordable Care Act. Through the involvement of top leadership and by employing leading and best practices, important progress on implementation has been made. This is a great tribute to the highly dedicated and professional men and women of the IRS who have devoted themselves to this project. I would be happy to answer your questions.

Chairman ISSA. Thank you.

I recognize myself now.

I want to start off by thanking you and the men and women of the IRS. I note that your job is a strenuous one, one that has a five-year term. I understand you are the third to have that term. And it was intended to take away the partisan perception, and I think you have done a good job of that. But I do have some questions, perhaps not so-called partisan, but maybe Pollyannaish.

You have done, the IRS has done a selective outreach based on ObamaCare or the ACA's benefits. You said it in your testimony. You sent out millions of post cards doing an outreach to educate people as to the law's benefit or tax credit to small business, correct?

Mr. SHULMAN. We did send out tax credits.

Chairman ISSA. Do you plan on sending post cards out to tell people about the tax increases?

Mr. SHULMAN. No.

Chairman ISSA. So you are only telling people, the IRS is only telling people about the good news and not telling them about tax increases. Aren't tax increases more something you need to know about in advance for planning than windfalls of money? I grew up in a neighborhood where that windfall is [foreign word], it is found money. This isn't what you need warning for. You don't need warning about good news; you need warning about tax increases, don't you?

Mr. SHULMAN. We do extensive outreach on all tax provisions, and we have started—

Chairman ISSA. But you are not sending any indication to small businesses about the tax increases they are going to see under ObamaCare?

Mr. SHULMAN. We have done extensive outreach and we do it based on looking at what's the best way to get the word out for different pieces. I think right now we are working with the preparer community and business community to work through, a, getting our systems in place in a way that works well, getting the interaction—

Chairman ISSA. Well, speaking of the systems, under ObamaCare Section 9002 you were required to deal with the W-2 forms, and yet you unilaterally delayed reporting requirements. In other words, this piece of bad news is not going out that otherwise would have made it clear that, again, tax increases, right?

Mr. SHULMAN. Are you referring to the requirement that employers—

Chairman ISSA. Put a value of health insurance benefits on the W-2.

Mr. SHULMAN. How much they paid for their health insurance.

Chairman ISSA. Right.

Mr. SHULMAN. No, we actually delayed the reporting requirement at the request of our information reporting committee that works with us regularly because they couldn't get their systems ready.

Chairman ISSA. They couldn't get their systems ready?

Mr. SHULMAN. We had a lot of feedback from the business community that—

Chairman ISSA. Well, let's go through that. There is Paychecks and ADP. They both got it ready. They are both able to do it.

Mr. SHULMAN. So I am——

Chairman ISSA. I am trying to understand. This was something that I think many people who want folks to understand, this is sort of the bad news again. This is letting people know how much is already being paid in. The question is: where did you get the authority to unilaterally delay? You are saying it is based on not being ready, and yet the vast majority of these things, either you could have allowed a waiver and yet still implemented for those who are ready, and if someone was using Paychecks or ADP they would have been ready and it would have happened, right?

Mr. SHULMAN. That is not my understanding. So my understanding is that this reporting, which I guess I am confused about it being bad news, this is just saying how much your current employer pays for your health insurance.

Chairman ISSA. Well, most Americans have no idea that health care costs as much as it does. This provision was one that I think Republicans wanted genuinely in there so people would understand just how expensive it is, how much is already being paid for. Having over the years had employees who left who were shocked when they had to pay their COBRA and they wanted to know what was wrong, and the answer was, Well, we were paying 90 percent of it, now you can see what you are not seeing from a tax standpoint.

Let me go through just one or two more questions. You said that the IRS would not be essentially dunning people who owed under the mandate, but is there anything that would prohibit you from assuming that the first \$1,000 owed under the mandate penalty which now is assessed to be a tax by our U.S. Supreme Court, and let's just say they refuse to pay it, is there anything that keeps you from considering that dollar one of taxable requirements and thus having the last dollar be owed?

In other words, if I pay in \$10,000 and I owe \$9,000 or \$8,000, and you simply make the assumption the first \$1,000 added is this tax that they didn't pay, is there any reason you wouldn't take it all and dun them for revenues owed? Is there anything that stops you from doing that?

Mr. SHULMAN. Let me try to answer the question. I'm not sure I understand it.

Chairman ISSA. If I don't pay my taxes, isn't it possible you could treat the \$1,000 mandated penalty like any other tax and dun me for it with penalty and interest?

Mr. SHULMAN. So if you don't pay that, what we would do is send out a letter. As you know, most people pay the taxes they owe on time. We would send out——

Chairman ISSA. But this is a tax that is not collected through withholding. If you assessed it as the first part of withholding, took it out of withholding, and then just simply dun me for being in arrears on my overall taxes, you could treat it, as long as there was \$1,000 of withholding, you would take it for this and then treat it as though I didn't have sufficient withholding. Couldn't you deal with that?

Mr. SHULMAN. So we would treat it as, you know, a penalty on your return. The statute is clear, and it is the only place the stat-

ute is clear, we can't do a lien or a levy, which is very rare, which we do way down the line. Beyond that, it would be part of your Federal tax obligation.

Chairman ISSA. I want to get this very clear, and I apologize for running over, but I haven't gotten the answer to the actual question, so let me be clear on the question. If I owe \$10,000 in normal taxes on income and I have this \$1,000 penalty, if you put the \$1,000 penalty at the end then you don't have the ability to levy or lien.

However, if you simply collect it as the first \$1,000 on my withholding, take it out, I now have a shortfall in my withholding, so now you are not levying against the penalty, you are levying against ordinary taxes you have already collected on the front end. There is nothing that stops you from taking that as the first dollar and then levying on the last dollar against income tax.

Mr. SHULMAN. I apologize. I want to be responsive. It will be part of your overall liability. If there is \$1,000 owed, there will be a \$1,000 carve-out that there could never be a lien on. I am confused about the withholding.

Chairman ISSA. And I am going to yield to the Ranking Member, but there clearly was a statement, no question at all, Federal exchanges were not covered in this law, in the letter of the law, and yet you have had a rule-making that covers it, covers it without legislative action but rather based on some loose intent.

The fact that we said that there is no levy, all you would have to do is collect this money off of the first \$1,000 of withholding and then the shortfall would actually be on other funds you could levy. Any creative accountant could come up with it. I am going to assume that the IRS will do so based on what your folks have chosen to do on something that was outside ObamaCare's right, which was subsidizing the Federal exchanges.

Mr. Ranking Member, I would ask unanimous consent you have an additional three minutes, so if you will tally eight minutes I will yield to the gentleman.

Mr. CUMMINGS. Thank you very much.

Commissioner Shulman, I hope that IRS employees are watching this, and I want to say to them publicly thank you, and I thank you. Let me tell you what I am thanking you for. As I listened to the last panel, I listened to Mr. Everson, and you heard most of his testimony, did you not?

Mr. SHULMAN. I did hear some of it.

Mr. CUMMINGS. Yes. And he talked a lot about his concerns and basically all but said it can't be done. And I have got to tell you that, as one who rose up from poverty to the Congress of the United States of America, I know that this Country, we can do anything we try hard enough to do. I know that. My own life has told me that.

When you started off your testimony today to talk about what you all have done already and what you did, I think you started back in 2008, you said you had to come in and do certain things. I just like the can-do attitude, because certainly if we stick with the naysayers I guess we won't get anything done. The fact is that what the people at IRS are doing in trying to make sure the law works properly will go a long ways towards helping a lot of people.

And I say this over and over again because I mean it. I am talking about people at IRS will end up helping people save their lives and save a lot of pain. And so I want to thank you all publicly for that can-do attitude. I know IRS gets a lot of bad comments. As a matter of fact, Government employees get a lot of bad comments. But when I hear things like what you just said, it just, in my mother's words, who is a former sharecropper, it just makes my heart glad.

Commissioner Shulman, in the earlier panel the Committee heard from Nina Olson, the National Taxpayer Advocate. In her testimony she explained that the IRS has made significant progress on rule-making and other areas. Let me read from her testimony. She says, "Since the enactment of ACA, the IRS has been working through the major challenges, making significant progress. The lead time provided by the ACA has been very helpful for the IRS, and at this point it appears the IRS has used the time well." Ms. Olson is very complimentary about your efforts over the past two years to ensure that the planning process is on track.

I would like to know your perspective. How did you approach the planning process over the past two years, and how would you evaluate your own efforts today?

Mr. SHULMAN. Well, the one thing, while the ACA is a substantial undertaking, the tax provisions for the IRS, you know, I come from a business background, and the one thing I would say generally is that what you need is proper planning, enough lead time, and proper resources to implement things.

In the world of tax, we have gotten used to, unfortunately, late legislation, retroactive legislation, and the one thing this law affords us is plenty of time to do implementation right.

We had to scramble to get some of the things done, some of the things that the Chairman referenced and we talked about, but the major pieces of the legislation where we have the most work to do, like setting up our infrastructure to make sure we distribute tax credits, the premium tax credits in conjunction with the exchanges, we had multiple years to do.

And so there is always room for improvement, but I think our team, both our team who had to work to do the planning, do the immediate implementation, and then build the IT systems, you know, I think they are well on track in doing, you know a good job, so I would give them a pretty good grade.

That said, we have got to keep our eye on the ball and with any piece of tax legislation we need to make sure we take it through and implement at the end.

Mr. CUMMINGS. Well, I hope that they know that they have a lot of grateful people who appreciate what they are doing.

On the first panel we heard a lot of concerns about data privacy, and that is a concern of mine. I know the IRS actually has a great record on protecting taxpayers' information. You may have heard some of that testimony.

Commissioner Shulman, what steps has the agency taken to ensure the security of taxpayer information going forward, and do you think that steps that you have taken will be sufficient? And what additional steps do you see being necessary?

Mr. SHULMAN. Let me say a couple things. First of all, this agency takes data security very, very seriously. And we have an excellent track record of protecting the American taxpayers' basic income data.

Second, I would just say there has been a lot of, both in the previous panel and also, you know, out there in the general dialogue, I think way overstatements of the risk of data security. I mean, this is not something wildly new to us. Right now we share data with States for child support information, with States for Medicaid, with States for tax information, and we have very strict safeguards around that data.

In this case, any data we exchange with States they have to have written procedures in place that we will look at. They have to agree to separate the data. They have to agree to have limited use of the data just for the purposes of the law. They need to train their people.

We have an Office of Data Privacy and Security that will go out and do audits to make sure it is right, and the Federal law takes tax data very seriously, and individual employees can be prosecuted for breaching tax data. That individual liability extends out to anyone we send data to.

And so this is nothing new for us. Obviously, it is an effort and we are going to have to do it, but I think the concerns about data security around this are overstated.

Mr. CUMMINGS. You sound like you take a lot of pride in IRS's efforts to keep the privacy of Americans' tax information private. You seem very proud of that. Are you?

Mr. SHULMAN. Well, A, I am very proud of it; B, it is a cornerstone of the tax system; C, we have done it a lot exchanging with States, and we haven't had major issues.

I will tell you a little story. My first day I showed up at the job I went to the Treasury Department and was sworn in by the Treasury Secretary. I came back, and the person waiting for me was the lawyer to explain the data privacy rules and the people who did the training for me. That is how seriously the agency takes this. They didn't brief me on our technology or our filing season, et cetera. The first thing I was briefed on was data security.

Mr. CUMMINGS. My last question, Ms. Olson spent a lot of time talking about the challenge for IRS with regard to communication, or communication strategy, taxpayer education about these new rules. Do you agree that taxpayer education is essential to the success of the implementation? And can you please explain how the IRS plans to educate the public about these new rules?

Mr. SHULMAN. Well, there are a few things. One is any time a tax law is passed we do a variety of things. We use social media to get information out. Sometimes we do direct communication, and 80 percent of taxpayers, and it is growing. Last tax season it was up actually over 85 percent, use either a paid professional preparer or tax software. And so a lot of the details of these rules, just like the details of the rest of people's tax forms, gets sorted out either when they are figuring out how to file or get sorted out, you know, with their preparer. So we do a lot of work with them, and we expect to expand our outreach.

I will also note that, because this issue has gotten, the Affordable Care Act has gotten so much attention by the media, you know, this is not something people are unaware of, and we are trying hard just to get the actual facts out, and we will keep that campaign up.

Dr. DESJARLAIS. [Presiding]. I thank the Ranking Member.

The Chair will now recognize himself for five minutes.

Mr. Shulman, thank you so much for being here today, because certainly we have several things we would like to clear up in regards to the initial drafting of the Affordable Care Act and the subsequent ruling by the IRS. I think you were listening to the first panel, and clearly there are some disagreements between Professor Jost and Mr. Cannon on whether or not the IRS ruling was illegal.

Why do you think, first of all, I think that the intent when the law was written it was clear that the Administration and the authors of the bill assumed that the States would set up exchanges. Certainly it was clearly mentioned numerous times throughout the language of the bill and there was not mention of the Federal exchanges. I think, one, that the health care law people were very leery of. I think 63 percent opposed this law when it was first presented or even passed. And I think Senator Baucus from Montana clearly wanted a national exchange, but I think the American people resoundingly rejected the thought of a national takeover of health care.

So the language was carefully crafted in the bill to mention State exchanges because State exchanges sounded much more palatable to people than a Federal takeover of health care.

So were you a little shocked, I guess, when I think there's only 14 States now that have decided to set up State exchanges? Was that kind of a surprise to you and something you hadn't anticipated?

Mr. SHULMAN. I guess I didn't follow, you know, the before and after as closely as that, so I had no reaction. I am watching how this goes. I mean, our main job is to try to implement the law that was written.

Dr. DESJARLAIS. Sure. Fair enough. Do you agree that when authorizing these premium assistance tax credits the Internal Revenue Code, Section 36(b), explicitly refers to health insurance exchanges established by the States under Section 1311?

Mr. SHULMAN. I think 36(b) has some contradictory language in it.

Dr. DESJARLAIS. Well, we can put up a slide. Is there anything unclear about that? Is there anything unclear? Does it mention Federal exchanges anywhere in that section?

Mr. SHULMAN. I am looking at the slide, but I am also aware of the whole statute, so I guess I—

Dr. DESJARLAIS. Okay. Do you recall it mentioning Federal exchanges?

Mr. SHULMAN. Excuse me?

Dr. DESJARLAIS. Are you aware, does it mention Federal exchanges or just State exchanges?

Mr. SHULMAN. Anywhere in 36(b), yes.

Dr. DESJARLAIS. In 1311. That is the slide. That is not the slide. We have another slide.

Mr. SHULMAN. I guess I watched the first panel and would agree that there is a lot of disagreement, and we obviously looked at the total statute and think we came to the correct legal reading.

Dr. DESJARLAIS. Okay. The plain meaning of the Rule 36(b), it is possible that the court could read the phrase an exchange established by the State under 1311 of ACA, this was the CRS ruling that the gentlelady from New York referred to in the first panel. It said that the exchange could be clear to not include an exchange establishment by the Federal Government. Indeed, the language seems to be straightforward on its face.

Are you aware of that CRS ruling?

Mr. SHULMAN. I am not aware of that.

Dr. DESJARLAIS. Okay. Well, do you agree that when authorizing those tax credits the IRC repeatedly refers to exchanges established by the State under Section 1311?

Mr. SHULMAN. I guess I am not aware of the—

Dr. DESJARLAIS. Okay. Well, it does repeatedly. Why did the IRS add the phrase, or in 1321 in the rule, do you believe this is a dramatic interpretation that in essence rewrites the law?

Mr. SHULMAN. No.

Dr. DESJARLAIS. Why do you say that?

Mr. SHULMAN. Maybe it would be helpful for you to hear how our rule-writing process works. I mean, our legal experts, career civil servants who are some of the best tax lawyers in the world, if not the best, take a look at statutes, look at the entirety of the statute, and try to come up with their best legal analysis.

Dr. DESJARLAIS. Okay. Well, basically we are set to scramble because this bill was set to be passed and go to conference, and it did not go to conference but rather reconciliation because the votes simply weren't there to pass the law. Scott Brown was elected and he was on his way in, so they had to rush this law. They knew it was imperfect. They knew that they couldn't force the States to set up exchanges.

The Federal Government doesn't have the power to force the States to do it, so they had to try, in essence, to coerce the States in a sense to set up these exchanges, and they didn't mention Federal exchanges on purpose because they wanted the States to do this. They wanted to kind of strong-arm the States to set up these exchanges, and they knew that they had to put out a bill with this language that was imperfect because if they didn't do it before the end of the year, and they did it on Christmas Eve, then they were going to have to deal with probably not passing the law at all.

So now you are tasked with basically cleaning up their mess, cleaning up their language, because it clearly wasn't in the bill. They referred to State-run exchanges repeatedly and left out the Federal exchanges, even in the reconciliation process. It simply wasn't in there.

So I think Mr. Cannon, his point is that the IRS way overstepped its bounds of separation of power, in essence wrote a huge tax increase, trillion dollar tax increase, that Congress did not intend, but this mess was created when the States didn't fall in line and set up the exchanges; isn't that true?

Mr. SHULMAN. No.

Dr. DESJARLAIS. Why do you say it is not true? It clearly is.

Mr. SHULMAN. I just disagree with Mr. Cannon. I think that this was the correct reading of the law. I have no idea what the reference is to a tax increase, but we are not concerned with that.

Dr. DESJARLAIS. You understand the statute. Does the statute ever say that the credits are available in Federal exchanges? Does it ever say that?

Mr. SHULMAN. There are sections of the statute that directly talk about a Federally-run exchange——

Dr. DESJARLAIS. Can you tell me where?

Mr. SHULMAN.—and the information to the IRS. In Section 1401, which is the same as 36(b), there's reference about information reporting of premium tax credits to the IRS from the Federal exchange. Look, I fully understand that you have a view on this and that we disagree. I think the law professors before on the panel before fleshed out the arguments on both sides. Our legal experts came down on the side that we came out with.

Dr. DESJARLAIS. I clearly disagree with you, because we know what the intent was. We know why this all came about, and I don't think the argument was clearly refuted. In fact, Professor Jost in several cases rescinded. First, he wanted to call it a drafting error, a scrivener's error. He retracted all those statements because they are scrambling to find a reason to justify what the IRS did.

Clearly, this issue is far from over. The companies in the States without State-run exchanges are going to challenge the IRS rule and this will probably end up in Federal court. I don't think there is any question about if; it is just a matter of when.

I see my time has expired. I will yield to the gentleman from Illinois, Mr. Davis.

Mr. DAVIS. Thank you very much, Mr. Chairman. And thank you, Commissioner.

There are a lot of assertions that people make and have made, and they have said that this is in the legislation, this is in the bill, it is going to cause people to do this and cause people to do that. And then when you look you can't find what they are basing their assumptions on.

I know that some opponents of the legislation have claimed that to implement this that the Internal Revenue Service has got to hire 16,000 new agents, enforcement agents. And you have said on numerous occasions that this is a made-up number with no basis in fact. As a matter of fact, some people have even compared the Internal Revenue Service to the Gestapo, as Mr. Everson pointed out in his testimony on the first panel, which is not only inaccurate but, quite frankly, unconscionable way beyond the pale, I think.

Do you agree that this type of non-information, of mis-information is damaging to the image of the agency? And is it true that you are going to have to hire all of these people to enforce provisions of the act?

Mr. SHULMAN. Sir, we have been incredibly transparent in what we need to implement this law. We put forward budgets and then sent to Congress the last three years of information, and then we put forward a budget this year. The budget we put forward this year, 92 percent of it is for infrastructure and technology to make sure that the act is executed. And so referring to this number 16,000 agents, I have no idea where anyone got that. That is not

going to happen. And, as I said, the major parts of this law are going to be handled, the compliance aspects, through correspondence.

You know, regarding unfortunate remarks about the IRS, all I would say is we have a very good track record of interacting with the American people in incredibly respectful ways. Right now the American customer satisfaction index, which is run by the University of Michigan, which looks at major companies across the globe as well as Government agencies, we have our highest rating ever at 73. Most people who interact with us send in a refund return, and within five to ten days get \$3,000 back from us, so I know that the words IRS sometimes conjure up things that people can make scary. The reality is, for most people we are a great service organization. So yes, it is unhelpful for people to use rhetoric, but I think our record stands for itself.

When you ask American citizens one by one in things like the American Customer Satisfaction Index, we get very high ratings.

Mr. DAVIS. There are also individuals who use this invasion of privacy. It is very interesting who some of them are. They are not people that I have known to be protecting the privacy of individual citizens in a lot of other instances and a lot of other ways, but they claim that the Internal Revenue Service is going to have access to individuals' private health information. Is that a need in order to enforce the provisions of the act?

Mr. SHULMAN. No. Absolutely not. What we will know and asked for, based on the law, is: do you have health insurance coverage? If so, for how many months? And what was the name of the insurance company?

Right now we get information about what's your income, who is your employer, how long were you employed? Do you own a house? Did you sell a house? Was there interest on this house? Do you have stocks or bonds? Did you buy them or sell them? And so we get lots of information, but we get the bare bones that we need to file a tax return.

I think it has been way over-stated our role in health care. I mean, we are basically going to facilitate the financial transactions that make this whole law work, but we are not going to have access to private individual health care information except for the fact of coverage.

Mr. DAVIS. Do you see individuals being locked up, incarcerated, liens placed on their homes or their properties or whatever it is that they might own in order to make sure that there is compliance?

Mr. SHULMAN. I mean, the minimum coverage provisions which say that you either need to have insurance or you pay a penalty, those specifically prohibit liens, levies, criminal prosecution, and so they are treated very different from other liabilities owed to the Federal Government.

Mr. DAVIS. So then many of these assertions are quite honestly inaccurate?

Mr. SHULMAN. Well, some of the ones you brought up, yes.

Mr. DAVIS. Well, thank you very much. My time is expired.

Mr. Chairman, I yield back.

Dr. DESJARLAIS. I thank the gentleman.

I think, being as we have a small dias today, I think we can go through a second round of questioning if you will indulge us.

Can you describe the universe of people who will be subject to the new HHS reporting requirements? We understand that it is expected that 20 million people will fall under these requirements; is that correct?

Mr. SHULMAN. I'm sorry? Which requirements?

Dr. DESJARLAIS. The HHS reporting requirements.

Mr. SHULMAN. I am not sure what the HHS reporting requirements are or what you are referring to.

Dr. DESJARLAIS. Okay. Well, under the HHS rules, isn't it true that for these Americans they will now be required to tell the State and the IRS when they change jobs within 30 days of the change?

Mr. SHULMAN. I think you are referring to the people who receive a premium tax credit?

Dr. DESJARLAIS. Okay. Isn't it true? Yes, you are referring to that.

Mr. SHULMAN. So the way the premium tax credit works is people go to an exchange. If they have not been offered affordable health care coverage by their employer, they may be eligible for a tax credit to help subsidize the purchase of insurance. And that is based on a number of factors, including their income.

If their income changes, they have an obligation to come back and say that the income changes so that the amount of the credit can be adjusted.

Dr. DESJARLAIS. Okay. And that is within 30 days?

Mr. SHULMAN. I am really not aware of the details of when that reporting back to the exchanges are, because that is not a piece of the act that we will be administering. That falls with, as you said, HHS and the exchanges.

Dr. DESJARLAIS. Okay. If they don't report the changes, assuming it is 30 days in the window, what are the consequences and how do you plan to enforce the rule?

Mr. SHULMAN. So the way the premium tax credit works, which I referred to in my opening comments, is people go to the exchange, they determine the eligibility for a credit and the amount of the credit. They receive the credit, an advance payment, and that payment is made directly to the insurance company, and then there is a true-up procedure when they file a tax return, much like a true-up of estimated taxes or a true-up of your withholding, and the way that it works is if they got too much of a credit up front they will owe some money back; if they got not enough, the Federal Government will owe them the true-up, so there is a true-up procedure that will be administered on the back end.

Dr. DESJARLAIS. According to your July 2010 report, IRS has fallen short of providing adequate taxpayer service in important areas. Given the massive scope of ObamaCare, is it likely the IRS customer service is going to get worse rather than better?

Mr. SHULMAN. I am not sure what the July 10 report is.

Dr. DESJARLAIS. The Taxpayer Advocate report.

Mr. SHULMAN. That is from the Taxpayer Advocate, who independently reports to Congress.

Dr. DESJARLAIS. Okay. Well, the question still stands about customer service. How do you anticipate that is going to be handled?

Mr. SHULMAN. We have had what I think is a very good track record of customer service with the resources we have been given, and I expect us to continue to deliver good customer service.

Dr. DESJARLAIS. So an hour-plus wait in your opinion is good customer service when people actually need to talk to somebody who knows something about an issue?

Mr. SHULMAN. We don't have an hour-plus wait on average.

Dr. DESJARLAIS. What would you say the wait is?

Mr. SHULMAN. It depends when you call. The wait can be as short as someone picks up the phone immediately and there is no wait, and it can be a lot longer. If people call at peak times, we tell them how long their wait is and they call back.

Dr. DESJARLAIS. Okay. From the National Taxpayer Association, for calls that require issues of expertise, the IRS track record is even worse. In March 2012 taxpayers calling IRS tax protection unit only reached IRS 11 percent of the time after an average wait time of an hour and six minutes.

Mr. SHULMAN. This was a very specialized line that had just been set up. It was under-staffed at the very beginning. Once we became aware of the problems we put new people on, and the year we have averaged 90 percent, and so that is a very short point in time, and when we see issues we correct them.

Dr. DESJARLAIS. I mean, I understand having pride in the agency that you oversee, but you can look in the camera and tell all the Americans watching that you feel the customer service within the IRS agency is good?

Mr. SHULMAN. I can do it the other way around, which is, as I mentioned, the American Customer Satisfaction Index, which goes out and asks Americans how are their interactions with the IRS, is at its highest level ever at 73 percent.

Dr. DESJARLAIS. That is not what the data says, and I think for the people watching they can probably make up their own minds. They don't have to take my opinion or yours.

My time has expired and I would be happy to yield or recognize now the Ranking Member for five minutes.

Mr. CUMMINGS. Thank you very much.

During one of our Subcommittee's hearings some business entities told us, Commissioner, that they were not sure which rules will apply to them and how they will comply with new requirements. I understand that some of these rules are still in progress, such as the rule on how to calculate full-time equivalent employees. Has the IRS engaged with businesses to ensure that programs and regulations are responsive to their concerns? And, number two, are there still misperceptions about IRS's role in implementing the health care reform bill?

Mr. SHULMAN. To the second one, any time there is, you know, a major tax bill we need to educate people. Frankly, until you start actually implementing, that is when people really focus their mind and understand.

With that said, we have been having extensive dialogue with the business community about the employer responsibility provisions of the law that we need to administer. As you mentioned, there's a couple things. One is there is a misperception that every business is subject to this. Ninety-six percent Of Americans' businesses have

less than 50 employees, and those people are totally exempt from the coverage requirements under the Affordable Care Act.

Second is we have really focused our time trying to put guidance out to the business community, so there is this notion of you need to have 50 full-time equivalent employees in order for the provisions to kick in, and so there's obvious questions about, okay, what is a full-time equivalent? What if I have 49 and then it goes to 50? What if somebody went from full time to part time? We have tried just to be very responsive, and so we have a look-back that says you can look back a year and say what did it look like the last year, and then you get a safe harbor for the next year so that people aren't going to continually be having to wrestle with this.

And so in the Affordable Care Act, but also really any time there is a major tax provision that is going to affect businesses, we have extensive dialogue with the business community, and what we try to do is make sure we put clear rules in place that will allow us to implement the law in the least burdensome manner possible to the business community.

Mr. CUMMINGS. Commissioner, as you mentioned earlier, the IRS will be involved in distributing billions of dollars in premium tax credits for people buying insurance in the exchange and administering the minimum essential coverage provisions of the Affordable Care Act. Therefore, the IRS will be in the position of verifying information provided by third parties such as insurers. Can you tell us a little bit about your real time tax initiative and what is it and when does it begin?

Mr. SHULMAN. So I guess two separate things. Yes, we are going to get information from insurance companies, information reporting very similar to what we get from brokerage companies today, banks, about interest information and home ownership and interest information from there.

The real time initiative is really something apart and separate from this. That is basically a concept that I have laid out that says a lot of the tax system runs after the fact, meaning people file, we then later match returns and we send them letters; that we actually think we could have a much less burdensome system for the American people and one that actually led to better compliance, as well, if we could get information returns at the same time as the tax returns and any time there was any confusion clear it up.

But the real time initiative that we have is something that is on a very different track. It is something that is just in the discussion phases, and we are getting lots of input, and it is really very separate from Affordable Care Act implementation.

Mr. CUMMINGS. Well, I am going to, just as my last question, the Chairman just asked you to look into the camera and talk about something. I am going to ask you to look into the camera, too, and that is: can you tell the American people why you feel comfortable that you are going to be able to do what is required of you, your agency, that is, under the Affordable Care Act? Do you feel comfortable, assuming that you get the resources, I'm sure.

Mr. SHULMAN. Yes. No, we feel very comfortable that the part of the Affordable Care Act which is in the Internal Revenue Code which we are responsible for, that it will be implemented well, it will be implemented on time, and people have my personal commit-

ment and the agency's broad commitment that we will do it in a way that minimizes burden on business and individuals and respects taxpayer rights and tries to facilitate, you know, a very good flow of information.

Mr. CUMMINGS. Thank you very much.

Dr. DESJARLAIS. [Presiding]. Thank you.

For the third round, we would like to go back to the exchange rule a little bit. I can understand your confidence when essentially the IRS was given unprecedented power in this case to basically rewrite a rule and bypass Congress as it has in this case, so I guess maybe it would be easier to be confident if I knew that I didn't have to go through Congress any more, I can just kind of make it up as I go.

But can you specify the exact language that says the subsidies go to exchanges created by the Federal Government?

Mr. SHULMAN. So a couple things. First, on your comment, we exercised the rule-writing authority that is delegated to the Secretary of the Treasury in every tax bill, and that is what we did. And there is actually a process in this Country that allows Congress to write the laws, we interpret them through rule, and implement them, and if there is a disagreement there is always the courts. So I don't think we have any special power under the Affordable Care Act that we don't have any time that we do rule-writing.

Section 1321 talks about the Federal Government will stand in for the State at times. Section 1401 talks about——

Dr. DESJARLAIS. Okay. Stop there. It says it may stand in, but it doesn't say it can issue tax credit, premium tax credits and it can't imply the tax against the employers. It doesn't say that, does it?

Mr. SHULMAN. Section 1401, the second cite you are asking for, is saying that each exchange, and explicitly references the Federal exchange, shall report information to the IRS regarding the premium credits that it pays. And so I very much agree with you that there is some contradictory language. Our lawyers' job is to say, taken in totality——

Dr. DESJARLAIS. You are not agreeing with me. I don't think it is ambiguous, sir. I don't think it is ambiguous. I think it is very clear. I think you are trying to twist it because you have to cover a gross misinterpretation that the States would set up exchanges, so that right now, to save this law, they couldn't save it the proper way by going to conference. They couldn't do that because Scott Brown was coming in and it was all going to fall apart, so they had to pass an imperfect bill, as Nancy Pelosi shared with all of us those famous words, we have to pass the bill to see what is in it.

They had to pass an imperfect bill, so now when the States didn't set up the exchanges we are having to go back around and try to find reasons for you to make this rule to include the Federal exchanges, which they did not intend to include. They wanted to force the States to do this. When the States didn't do it, now we have this problem that we are here talking about today.

Who initiated the rule for the exchange rule? Did the rule initiate at IRS or at the Treasury?

Mr. SHULMAN. The way our rule-writing works is that lawyers at the IRS look at statutes, come up with their best interpretation. I

have to sign off on rules, as does the Assistant Secretary of Tax Policy.

Dr. DESJARLAIS. How many times did you meet with the Treasury to discuss this rule?

Mr. SHULMAN. Excuse me?

Dr. DESJARLAIS. How many times did you meet with the Treasury to discuss this rule?

Mr. SHULMAN. I meet with the Treasury Department of Tax Policy and their leadership on a regular basis. I have no idea how many times we actually talked about this rule. We talk about a lot of things. The tax code is very big and very complex.

Dr. DESJARLAIS. It is, and it needs to be reformed.

Was there any pressure from the Treasury Department to issue a rule that went beyond the statutory authorization?

Mr. SHULMAN. I never felt any pressure on this rule. You know, my judgment on the rule was based on speaking with our lawyers and coming up with what we thought was the correct legal reading.

Dr. DESJARLAIS. Have you ever done anything like this before?

Mr. SHULMAN. Excuse me?

Dr. DESJARLAIS. Have you ever done something like this before?

Mr. SHULMAN. The Commissioner of Internal Revenue Service is continually consulting with the lawyers of the Internal Revenue Service and putting out regulations to interpret statutes. It is a major part of the job.

Dr. DESJARLAIS. Okay, Mr. Shulman, and I know you are just trying to do your job. I will just close with one last question. The IRS will be responsible for collecting thousands of dollars from employers under the employer mandate. If the IRS makes mistakes, how can employers protect themselves from having to pay hundreds of thousands of dollars in error?

Mr. SHULMAN. We have very laid-out, traditional administrative processes, and so, if we think somebody owes more taxes the first thing we do is try to work with them. If they disagree, they have, you know, very established appeals rights to supervisors. Then there is actually an administrative appeals process, our Office of Appeals, and then there is always the courts. And so there is a lot of avenues for people to disagree with us, and that is, you know, part of this Country.

Dr. DESJARLAIS. Okay. So you are saying that your plans for an appeal process for employers is already in place?

Mr. SHULMAN. It will be, you know, plans that we have, you know. It is not plans; it is procedures that we have in place, long-established procedures to make sure the tax code is administered in a fair and even-handed manner.

Dr. DESJARLAIS. So we don't really know how employers will be able to appeal their penalties at this point?

Mr. SHULMAN. If a penalty is assessed, most people voluntarily pay. If they disagree, whoever made the determination for the assessment they can always talk with their supervisor, and those processes are well enunciated in the Internal Revenue Manual. They can then go to our appeals function, which is an independent function much like an administrative court inside the IRS. And if they still disagree after those two steps, they can go to the courts.

Dr. DESJARLAIS. Okay. Identity theft is a big problem, and information sharing in ObamaCare makes it worse. That is a report that just came out from the IRS today.

Mr. SHULMAN. That is incorrect. Identity theft is a problem in this Country, but there has never been an allegation that there is a problem with information for identity theft coming from the IRS.

Dr. DESJARLAIS. This is the text from the ruling issued today. In a new report to be issued Thursday, the Inspector General for the IRS says the tax thieves are stealing the identity of taxpayers and filing bogus returns on their behalf and collecting fraudulent refunds as a result. That is about \$21 billion in fraudulent tax refunds over the next five years. Are you not aware of that?

Mr. SHULMAN. I am aware of that report, but I want to be very clear: people get their purse stolen in a mall, someone has personal information, and then they file a return with us. Or someone has access to an employer database and they steal information and file a return with us. There are no allegations in that report or other places that information is being taken out of the IRS for identity theft purposes.

Further, I have read that report. That report is very clear that the problems with identity theft mostly are systemic, and there is a variety of things that we have asked Congress to do to give us powers that haven't passed.

Dr. DESJARLAIS. So you don't think it is possible that with all the new information you have got to collect regarding ObamaCare, that this problem could get worse?

Mr. SHULMAN. I think connecting identity theft as a problem in this Country and the Affordable Care Act would be totally irresponsible to connect those two.

Dr. DESJARLAIS. Interesting. All right. Well, I tell you what, I thank you very much for your testimony and your patience in going through three rounds of questioning.

I would like to thank all of our witnesses today for taking time from their busy schedules to appear before us today.

The Committee stands adjourned.

[Whereupon, at 12:43 p.m., the committee was adjourned.]

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Opening Statement

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JACKIE SPEER, CALIFORNIA

Hearing on "IRS: Enforcing ObamaCare's New Rules and Taxes"

August 2, 2012

The Affordable Care Act is a landmark achievement that will save huge sums of money for our nation while extending health insurance coverage to millions of people.

Last month, the Congressional Budget Office issued a report finding that the Affordable Care Act will extend health insurance coverage to 30 million people who do not have it today. That is an amazing accomplishment that our nation should be proud of.

In addition, our constituents are already seeing how the Affordable Care Act is putting money back in their pockets. This week, insurance companies are returning to their customers more than \$1 billion in the form of rebates and lower premiums. That is a direct result of the Affordable Care Act.

Just yesterday, women in private health insurance plans became eligible for life-saving, preventive health screenings—with no co-pays. This is part of the Affordable Care Act's comprehensive effort to save money by focusing on prevention. It also addresses the historic disparities women face when paying for healthcare.

The Affordable Care Act also has begun to ensure that seniors have access to preventive care, young adults have access to insurance on their parents' plans, and individuals are no longer subject to lifetime limits on care.

While all these reforms are being realized now, many significant changes are yet to come. The Internal Revenue Service is a key agency charged with implementing many of the Affordable Care Act's provisions by 2014, including minimum coverage requirements and tax credits for individuals purchasing health insurance on the exchanges.

This is a considerable undertaking for the IRS. Experts from the Government Accountability Office, the Inspector General's office, and the National Taxpayer Advocate have reviewed IRS efforts to date, and they have concluded that the IRS is on the right track to successfully implement the law.

For example, GAO issued a report that says this: the IRS “generally followed leading practices for implementing such a large program, particularly at the level of individual offices and projects,” emphasizing that “top leadership has been involved.”

In addition, the Inspector General issued a report that says this: “appropriate plans had been developed to implement tax-related provisions of the ACA using well-established methods for implementing tax legislation.”

And in her testimony today, Nina Olson, the National Taxpayer Advocate, says this: “Since ACA enactment, the IRS has been working through the major challenges, making significant progress. ... The lead-time provided by the ACA has been very helpful for the IRS, and at this point, it appears the IRS has used the time well.”

Certainly, there are significant challenges in implementing this law. And as the IRS moves forward, it benefits greatly from the continued rigorous oversight and recommendations from GAO, the IG, and the National Taxpayer Advocate.

At the same time, we recognize that the IRS has been actively planning to implement the Affordable Care Act for more than two years, and it has already implemented many of the provisions successfully. For the challenges that remain, the IRS is working closely with taxpayers, the business community, and the insurance industry to ensure that its policies are responsive to consumers and consistent with the intent of Congress in passing the law.

Today, the Committee is faced with a choice. Do we act constructively or destructively? Do we build up or tear down? Do we help or hurt?

On one hand, we could work with the IRS and its oversight entities to ensure that the Affordable Care Act is successfully implemented, particularly now that the Supreme Court has ruled that it is constitutional. On the other hand, we could try to exploit any and all ways to bring down this law or starve the IRS of the resources it needs to do its job.

I personally hope we pursue the first approach. However, Republicans have introduced legislation to do the second. The Congressional Budget Office has examined the Republican bill to repeal the Affordable Care Act and concluded that it would increase the federal budget deficit by \$109 billion over the next ten years.

It is time to accept the Affordable Care Act, to accept the Supreme Court decision, and to accept the billions of dollars in savings this law will bring for our citizens. I look forward to today’s testimony, and I thank our witnesses for being here.

Congress of the United States
Washington, DC 20515

November 4, 2011

Hon. Douglas Shulman
 Commissioner of Internal Revenue
 Department of the Treasury
 1111 Constitution Avenue, NW, Room 3241
 Washington, DC 20224

Dear Commissioner Shulman:

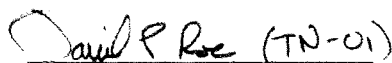
Recent reports indicate that proposed rule REG-13149-10 (rule) released on August 17, 2011 relating to the federal health insurance premium assistance tax credits (tax credits) included in the Patient Protection and Affordable Care Act (PPACA, P.L. 111-148) contradicts the explicit statutory language describing individuals' eligibility for receipt of these tax credits.

Section 1401(b)(2)(A) of Subtitle E of Title I of PPACA states that the tax credit amount determined under this section shall be provided to eligible individuals in a qualified health plan who are "enrolled in through an Exchange established by the State under [Section] 1311 of the Patient Protection and Affordable Care Act..." However, the rule expands individuals' eligibility for tax credits beyond PPACA's explicit text to individuals enrolled in qualified health plans who reside in states which the federal government has established an Exchange pursuant to PPACA's authority under Section 1321. Specifically, the rule states "The proposed regulations provide that a taxpayer is eligible for the credit for a taxable year if the taxpayer...is enrolled in one or more qualified health plans through an Exchange established under section 1311 or *1321* [emphasis added] of the Affordable Care Act [PPACA]..."¹

Section 1 of Article I of the U.S. Constitution vested the Congress of the United States with the power to enact legislation. Federal administrative agencies like the Internal Revenue Service do not have the authority under our Constitution to propose regulations which contravene the explicit statutory text of dually-enacted public laws. Therefore, the proposed rule—allowing individuals enrolled in qualified health plans through a federally-operated exchange to receive a tax credit—is in violation of Section 1401(b)(2)(A) of PPACA.

We request that you amend the proposed rule's language to be consistent with PPACA's statutory text. Should your agency fail to make such a change, we will be left to consider a legislative solution that enforces Congressional intent.

Sincerely,

 (TN-01)

 (TN-04)

¹ Page 50934 of the Federal Register/Vol. 76, No. 159/Wednesday, August 17, 2011/Proposed Rules

Carl (Bm GA-10

Mazha Blackburn TN-07

W. Cadd Abin MO-02

Larry Bushon IN-06

Mac TLo TX-13

Cynthia (P) Summis

Brett Hathorn

Pat Chye TX-26

Diane Black TN-16

John Pitts PA-16

Reid J Kiddle WI-8

Shirley Penn IN-16

Mark IN-3

Quico Cansero TX-23

Paul Fromm (TX-17)

John (Shirley) Dick

Pat TLo TX-11

Sam Co. 16-4

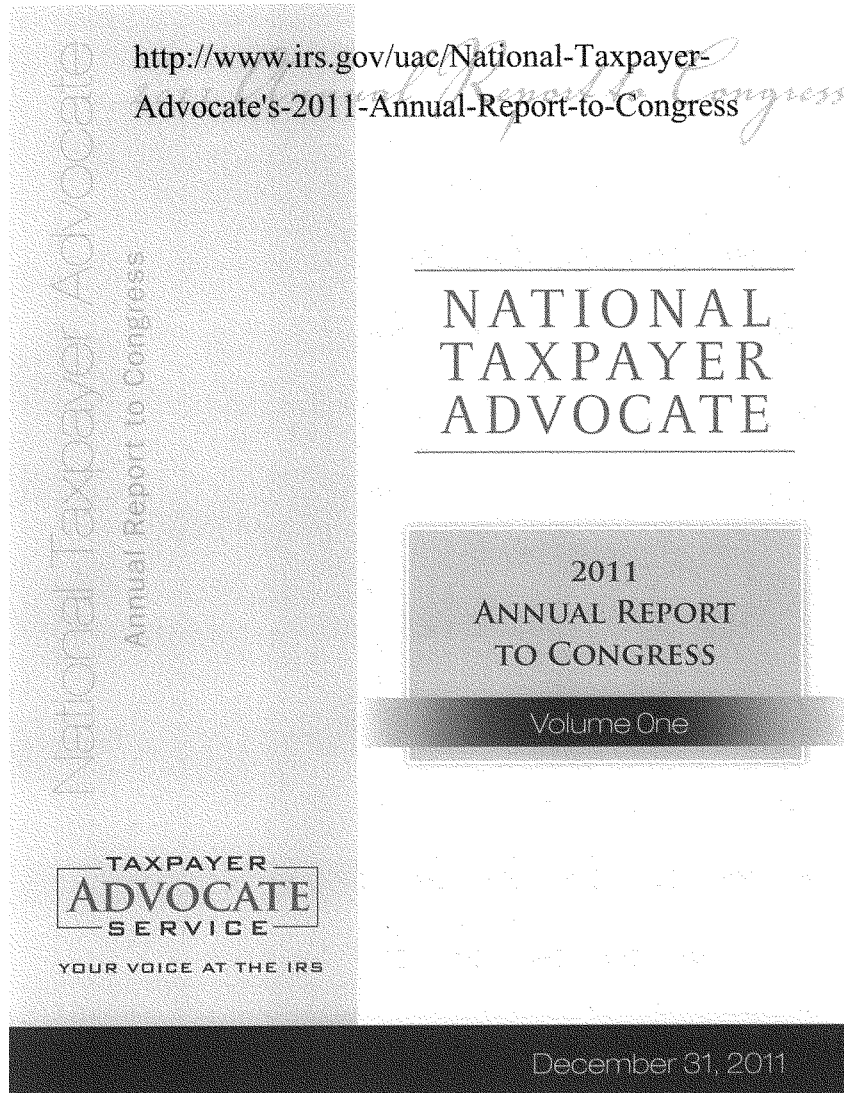
Bill Casey FL-15

Gilly Long

John Kingston GA-3

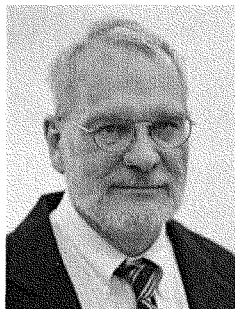
Robert (B) Adcock 16-4

<http://www.irs.gov/uac/National-Taxpayer-Advocate's-2011-Annual-Report-to-Congress>



Yes, the Federal Exchange Can Offer Premium Tax Credits

September 11, 2011 by [Timothy Stoltzfus Jost](#) · [12 Comments](#)
 Filed under: [Health Law](#), [Law](#)



Whatever else the Affordable Care Act may accomplish, it has provided endless entertainment for law professors. The latest ACA kerfuffle involves the discovery by critics of the ACA of an ACA drafting error that would seem to deprive millions of uninsured Americans of tax credits to purchase health insurance and invalidate regulations recently proposed by HHS and the Treasury Department. The mistake is found in section 1401 of the ACA, which creates a new section 36B of the IRC. Two subsections of 36B ((b)(2)(A) and (c)(2)(A)(i)) suggest that premium tax credit eligibility under the ACA depends on the applicant being enrolled in a qualified health plan “through an Exchange established by the State under section 1311.” This would in turn suggest that individuals enrolled in a qualified health plan through a federal exchange established under section 1321(c) would not be eligible for premium tax credits, contrary to the recent proposed regulations.

That this is a drafting error is obvious to anyone who understands the ACA. Section 1311 of the ACA requests the states to establish American Health Benefit Exchanges and sets out the duties of the exchanges. Section 1321 of the ACA, however, provides that if a state elects not to establish and exchange or fails to do so, HHS must “establish and operate” an exchange in such a state and “take such actions as are necessary to implement” the other requirements of title I of the ACA, which includes section 1401. There is no coherent policy reason why Congress would have refused premium tax credits to the citizens of states that ended up with a federal exchange. None of the CBO reports scoring the ACA suggest that premium tax credits would only be available through 1311 state exchanges and not through 1321 federal exchanges. It is, finally, highly unlikely that the House, whose bill included only a federal exchange, would have approved a bill that only provided tax credits through state exchanges but not through the federal exchange.

No one pretends that the ACA is a model of statutory drafting. The bill, for example, contains three section 1563's. No one intended the current ACA to become the final law. It was the

Senate bill, enacted after the House bill, which was to go through conference before the final ACA was enacted. The election of Scott Brown in Massachusetts, and the adamant refusal of the Republicans to allow the legislation to become law without a supermajority in the Senate, doomed efforts to craft a final bill. Of course, major pieces of legislation are often replete with drafting errors. They are commonly followed by technical correction bills, which are often adopted by unanimous consent. If Congress were functioning as a normal deliberative governing body rather than as the legislative equivalent of trench warfare, errors in the ACA would long ago have been fixed.

But now we seem to be stuck with the textualists delight: a statute whose words clearly say what Congress clearly did not mean.

Is there a way out of this quandary? One possibility is to simply recognize that this is a drafting error. The Supreme Court has occasionally recognized that it is appropriate to exercise common sense in recognizing that “a busy Congress is fully capable of enacting a scrivener’s error into law.” *Koons Buick Pontiac, GMC, Inc. v. Nigh*, 543 U.S. 50, 65 (2004) (Stevens concurring). But we do not need to rely on the courts to correct this error. Congress corrected it itself.

Four days after Congress passed the Patient Protection and Affordable Care Act, it enacted the Health Care and Education Reconciliation Act of 2010. Section 1004 of HCERA amended section 36B(f) of the IRC to impose on exchanges established under section 1311(f)(3)—that is, state exchanges—and under section 1321(c)—that is federal exchanges, the obligation to report to the IRS and to the taxpayer information regarding tax credits provided to individuals through the exchange. In this later-adopted legislation amending the earlier-adopted ACA, Congress demonstrated its understanding that federal exchanges would administer premium tax credits.

Section 36B(g) gives the Secretary of the Treasury the responsibility of issuing regulations to implement section 36B. This includes the authority to reconcile ambiguities in the statute, such as the inconsistency between subsections (b), (c), and (f) of 36B. In proposed regulations published on August 17, Treasury has proposed to recognize as eligible for premium tax credits any individual who is enrolled in a qualified health plan through an exchange and who meets other eligibility requirements, and adopts the HHS proposed definition of an exchange, which includes a federally-assisted exchange.

Under the Chevron rule, this official construction of an ambiguous statute should be accorded deference by any reviewing court. In fact, however, there will be no judicial review of this determination. It is not possible to conceive of a person who would be injured in fact by this interpretation of the rule such that they could present a case or controversy under Article III. The possibility, expressed by some, that a state official might be able to challenge the IRS rule should be put to rest by Thursday’s [Fourth Circuit ruling](#), reaffirming long established Supreme Court precedent holding that state officials do not have the authority to serve as “roving constitutional watchdog[s].”



**CONGRESSIONAL DISTRIBUTION
MEMORANDUM**

July 23, 2012

From: Jennifer Staman and Todd Garvey, Legislative Attorneys

Subject: Legal Analysis of Availability of Premium Tax Credits in State and Federally Created Exchanges Pursuant to the Affordable Care Act

This memorandum has been prepared for distribution to more than one congressional office.

This memorandum analyzes whether premium tax credits available to certain individuals under §36B of the Internal Revenue Code, as established under §1401 of the Patient Protection and Affordable Care Act (ACA),¹ would be available for individuals who participate in federally created health insurance exchanges. It has been argued that, under this section, premium tax credits would only be available in exchanges established by a state and not those established by the federal government. This memorandum provides a brief background on relevant provisions of ACA, addresses considerations that a court could take into account in interpreting the statutory language of §36B of the Act; and, finally, discusses how regulations implementing the premium tax credit could be evaluated.

Background

As part of ACA's intended goal of improving the private health insurance market and accessibility for health coverage, ACA specifies that by January 1, 2014, each state must establish an American Health Benefit Exchange ("exchange") that is either a state governmental agency or a nonprofit entity, in order to provide health coverage to qualified individuals and/or employers.² ACA generally provides that if a state does not elect to establish an exchange, or if the Secretary of Health and Human Services (HHS) determines that an electing state will not have an operational exchange by January 1, 2014, or has not taken certain specified actions, the Secretary must establish and operate an exchange within the state.³

In order to assist individuals in purchasing health insurance in an exchange, §36B of the Internal Revenue Code, created by §1401 of ACA, provides that, beginning in 2014, certain lower income taxpayers may receive a refundable tax credit that is paid directly to an insurer and applied toward the cost of the health insurance premium.⁴ In general, there are two principal factors one must consider in determining whether

¹ P.L. 111-148 (2010). ACA was amended by the Health Care Education and Reconciliation Act of 2010, P.L. 111-152 (2010), (HCERA). These Acts will be collectively referred to in this memorandum as "ACA." It should be noted that section 1401 of ACA has been subsequently amended, but these amendments are not relevant to this analysis.

² P.L. 111-148, §§1311(b)(1), 1311(d)(1).

³ P.L. 111-148, §1321(c).

⁴ 26 U.S.C. § 36B.

a taxpayer will be eligible for a premium tax credit: (1) whether the taxpayer meets the income and other requirements for the credit;⁵ and (2) whether any months during the taxable year qualify as “coverage months” for the taxpayer. With respect to this second requirement, in order for a taxpayer to receive a health insurance premium credit under ACA, at least one month in the year must qualify as a coverage month for the taxpayer.⁶ The term “coverage month” in §36B means the following:

[W]ith respect to an applicable taxpayer, any month if--

(i) as of the first day of such month the taxpayer, the taxpayer’s spouse, or any dependent of the taxpayer is covered by a qualified health plan ... *enrolled in through an Exchange established by the State under section 1311 of the Patient Protection and Affordable Care Act ...*⁷

In addition, the amount of the premium tax credit is equal to the sum of the “premium assistance credit amount” for each coverage month the taxpayer experiences during the taxable year. The premium assistance credit amount is defined as the amount equal to the lesser of--

(A) the monthly premiums for such month for 1 or more qualified health plans offered in the individual market within a State which cover the taxpayer, the taxpayer’s spouse, or any dependent ... of the taxpayer *and which were enrolled in through an Exchange established by the State under 1311 of the Patient Protection and Affordable Care Act, or*

(B) the excess (if any) of--

(i) the adjusted monthly premium for such month for the applicable second lowest cost silver plan with respect to the taxpayer, over

(ii) an amount equal to 1/12 of the product of the applicable percentage and the taxpayer’s household income for the taxable year.⁸

It has been argued that, based on this language in §36B, i.e., “an Exchange established by the State under section 1311 of [ACA],” premium tax credits are not available to taxpayers in exchanges created by the federal government.⁹ However, in May 2012, the Internal Revenue Service (IRS) rejected this interpretation in final regulations related to the premium tax credit, providing that premium tax credits are available to taxpayers who obtain coverage in both state and federally facilitated exchanges.¹⁰ The preamble to the regulations explains the IRS’s position that the statutory language of §36B supports this interpretation, and provides further that “... the relevant legislative history does not demonstrate that

⁵ In order to be eligible for a premium credit, a taxpayer’s household income must be between 100% and 400%, inclusive, of the federal poverty line (FPL) for the taxpayer’s family size. 26 U.S.C. § 36B(c)(1). Individuals with income below 100% of the FPL are ineligible for a premium credit, but may qualify for assistance under Medicaid. An exception is made for lawfully present aliens with income below 100% of the FPL, who are ineligible for Medicaid on account of their alien status. 26 U.S.C. § 36B(e). These taxpayers will be treated as though their income is exactly 100% of FPL for purposes of the credit.

⁶ 26 U.S.C. § 36B(b)(1). It should also be noted that any month during which an individual is eligible for other minimum essential coverage would not be counted as a coverage month. Examples of other minimum essential coverage include, but are not limited to, affordable employer provided coverage, Medicare, and Medicaid.

⁷ 26 U.S.C. § 36B(c)(2) (emphasis added).

⁸ 26 U.S.C. § 36B(b)(2)(A)-(B) (emphasis added). It should be noted that the reference to the “silver plan” in subsection (B) refers to one that is offered in the “same Exchange” as plans described in subsection (A). 26 U.S.C. § 36B(b)(3)(B).

⁹ See, e.g., Wall Street Journal, Health Law Opponents Challenge Tax Credit, July 16, 2012, available at <http://online.wsj.com/article/SB10001424052702303933704577531271643114572.html>.

¹⁰ Department of the Treasury, Internal Revenue Service, Health Insurance Premium Tax Credit, 77 Fed. Reg. 30377 (May 23, 2012).

Congress intended to limit the premium tax credit to State Exchanges,” and that this reading of the language of §36B “is consistent with the language, purpose, and structure of section 36B and the Affordable Care Act as a whole.”¹¹

Potential Statutory Interpretation of Section 1401 of ACA

In general, the starting point for courts in interpreting the meaning of a statute is the language of the statute itself. The Supreme Court often recites the “plain meaning rule,” that if the language of the statute is clear and unambiguous, it must be applied according to its terms. As the United States Supreme Court stated in *Connecticut National Bank v. Germain*:

[I]n interpreting a statute a court should always turn first to one cardinal canon before all others. We have stated time and again that courts must presume that a legislature says in a statute what it means and means in a statute what it says there When the words of a statute are unambiguous, then, this first canon is also the last: judicial inquiry is complete.¹²

Applying the plain meaning rule to §36B, it is possible that a court could read the phrase “an exchange established by the State under 1311 of ACA,” as being clear to not include an exchange established by the federal government. Indeed, this language seems to be straightforward on its face, which has perhaps led some commentators to suggest that the lack of reference to a federally created exchange could have been a drafting error.¹³ However, courts often assume that the language Congress employs, including additions and omissions to a particular statute, is intentional.¹⁴ Therefore, a court may be inclined to find that §36B presents a clear statement regarding the types of exchanges in which taxpayers may receive a premium tax credit, and may not look to any additional factors in its analysis.¹⁵

On the other hand, it is possible that a court could find that it is unable to rely on a plain meaning interpretation of §36B, perhaps finding the language to be ambiguous.¹⁶ In examining whether §36B is

¹¹ *Id.* at 30378.

¹² 503 U.S. 249, 254 (1992)(citations omitted). *See also* Caminetti v. United States, 242 U.S. 470, 485 (1917) (“It is elementary that the meaning of a statute must, in the first instance, be sought in the language in which the act is framed, and if that is plain, and if the law is within the constitutional authority of the law-making body which passed it, the sole function of the courts is to enforce it according to its terms.”).

¹³ *See e.g.*, Brett Ferguson, *IRS Rule Related to Employer Mandate May Be Next Challenge in Courts, Critics Say*, BNA Health Care Policy Report, July 16, 2012 (statements of Judith Solomon).

¹⁴ *See generally*, Russell v. United States, 464 U.S. 16, 23 (1983)(“Where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion”).

¹⁵ It should be noted that there seems to be general consensus that the plain meaning rule aptly characterizes interpretational priorities (statutory language is primary, other considerations of intent and purpose secondary). However, agreement on the basic meaning of the plain meaning rule—if it occurs—does not guarantee agreement in the rule’s application. For example, there have been cases in which Justices of the Supreme Court have agreed that the statutory provision at issue is plain, but have split 5-4 over what that plain meaning is. *See, e.g.*, *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479 (1985) (disagreement over the scope of civil RICO). *See also* *Corley v. United States*, 556 U.S. 303 (2009). There are other cases in which strict application is simply ignored: courts, after concluding that the statutory language is plain, nonetheless look to legislative history, either to confirm that plain meaning, or to refute arguments that a contrary interpretation was “intended.” *See, e.g.*, *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200, 209 (1994); *see also* *Darby v. Cisneros*, 509 U.S. 137, 147 (1993) (“Recourse to the legislative history of §10(c) is unnecessary in light of the plain meaning of the statutory text.” The Court considered the legislative history, nevertheless, and found nothing inconsistent between it and the Court’s reading of statutory language.). For general information on the plain meaning rule, *see* CRS Report 97-589, *Statutory Interpretation: General Principles and Recent Trends*, by Larry M. Eig.

¹⁶ According to a leading statutory construction treatise, “[a] statute is ambiguous when it is capable of being understood by reasonably well-informed persons in two or more different senses.” SINGER & SINGER, *STATUTES AND STATUTORY* (continued...)

ambiguous, a court may look, for example, to the definition of “exchange” in ACA. ACA defines the term “exchange” as the following:

EXCHANGE.—The term ‘Exchange’ means an American Health Benefit Exchange established under section 1311 of the Patient Protection and Affordable Care Act.¹⁷

Section 1311 of ACA, as referenced in this definition, seems to only address the creation of state-established exchanges. The section does not explicitly speak to federally created exchanges -- those are addressed in §1321 of ACA. However, section 1321 of ACA also uses the term “exchange”: it states that the Secretary of HHS must establish an “exchange” if a state should fail to take certain specified actions:

(c) Failure to establish Exchange or implement requirements.

(1) In general. If--

(A) a State is not an electing State ; or

(B) the Secretary determines, on or before January 1, 2013, that an electing State--

(i) will not have any required Exchange operational by January 1, 2014; or

(ii) has not taken the actions the Secretary determines necessary to implement [certain requirements]--

the Secretary shall ... establish and operate such Exchange within the State and the Secretary shall take such actions as are necessary to implement such other requirements.

Plugging in ACA’s general definition of “exchange” into §1321 above arguably links a federally created exchange to one established by a state pursuant to the requirements of §1311. Thus, it may be questioned whether, based on the definition of “exchange,” a federally created exchange should in some way be synonymous with one created by a state under §1311 and how this could affect the interpretation of §36B.

If a court considers the language in §36B to be ambiguous, it may look at legislative history and other extrinsic aids to determine congressional intent. While a survey of the legislative history of ACA with respect to §36B is beyond the scope of this memorandum, some have asserted that Congress intended to have premium tax credits only available in state-run exchanges in order to incentivize states to establish an exchange.¹⁸ Conversely, others may claim that premium tax credits were part of ACA’s goal of improving access to health care, which is arguably undermined if the availability of premium credits is limited to state-run exchanges. It has also been noted that reports by the Congressional Budget Office and the Joint Committee on Taxation assumed in their analyses of the legislation that premium tax credits

(...continued)

CONSTRUCTION (Sutherland Stat. Const.) (7th ed.), vol. 2A, § 46.4 (2007).

¹⁷ P.L. 111-148, § 1563(b). Section 1563(b) of ACA, entitled Conforming Amendments, amends section 2791 of the Public Health Service Act. Section 1551 of ACA states that unless specifically provided for otherwise, the definitions contained in section 2791 of the Public Health Service Act shall apply with respect to title I of ACA (which contains the provisions related to exchanges).

¹⁸ See Julie Rovner, *Could the Health Law End Up Back in Court? Opponents Think So*, National Public Radio Health Blog, July 18, 2012, available at <http://www.npr.org/blogs/health/2012/07/18/156936766/could-the-health-law-end-up-back-in-court-opponents-think-so>.

would be available in both state and federally run exchanges.¹⁹ Arguments such as these may be explored by a reviewing court.

Another important canon of statutory construction provides that parts or sections of statutes or Acts should be evaluated in connection with other parts and sections as one “harmonious whole” – requiring examination of not just one particular provision, but the broader legislative scheme in which the provision is included.²⁰ A court relying on this canon may look to §36B(f)(3), addressing certain reporting requirements with respect to the premium tax credit. This subsection states:

“(3) INFORMATION REQUIREMENT.— Each Exchange (or any person carrying out 1 or more responsibilities of an Exchange under section 1311(f)(3) or 1321(c) of the Patient Protection and Affordable Care Act) shall provide the following information to the Secretary and to the taxpayer with respect to any health plan provided through the Exchange ...

“(B) The total premium for the coverage without regard to the [premium tax] credit under this section or cost-sharing reductions under section 1402 of such Act.

“(C) The aggregate amount of any advance payment of such credit ...

“(E) Any information provided to the Exchange, including any change of circumstances, necessary to determine eligibility for, and the amount of, such credit.

Unlike the language in question, §36B(f)(3) addresses reporting requirements which seem to explicitly apply to both state and federally created exchanges (i.e., “Each Exchange (or any person carrying out 1 or more responsibilities of an Exchange under section 1311(f)(3) or 1321(c) of the Patient Protection and Affordable Care Act”). While one may argue that it is possible for this information requirement to be fulfilled without premium credits being provided to individuals participating in federally run exchanges (i.e., it could be reported to the Secretary that no taxpayer in a state with a federally run exchange received a credit), others may argue that if you look at this provision along with the other language in §36B, this demonstrates congressional intent to have premium tax credits available to taxpayers in both state and federally created exchanges, or, perhaps highlights a discrepancy that must be resolved by a court or the IRS in implementing the provision.

It is also possible that a reviewing court could examine how the language in §36B arises in other provisions of ACA and whether those other applications provide insight as to congressional intent.²¹ The phrase “an Exchange established by the State under 1311 of [ACA]” arises numerous times throughout the Act. For example, §2001(b) of ACA, entitled “Maintenance of Medicaid Income Eligibility (MOE),” provides that states with Medicaid programs in effect on the date of enactment of ACA must maintain their programs with the same eligibility standards, methodologies, and procedures until the Secretary of

¹⁹ See, e.g., Timothy Jost, *Implementing Reform: Funding And Flexibility For States On Exchanges*, Health Affairs Blog (Nov. 30th, 2011), available at <http://healthaffairs.org/blog/2011/11/30/implementing-reform-funding-and-flexibility-for-states-on-exchanges/>.

²⁰ See Sutherland, note 17 *supra*, at 201. Also, as the Supreme Court has noted, “[i]t is a fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme. ... A court must therefore interpret the statute ‘as a symmetrical and coherent regulatory scheme,’ and ‘fit, if possible, all parts into an harmonious whole.’” *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 133 (2000).

²¹ However, it is important to note that it is possible for two statutory provisions with similar language to be interpreted differently. See, e.g., *General Dynamics Land Systems, Inc. v. Cline*, 540 U.S. 581 (2004), where the Court determining that the word “age” is used in different senses in different parts of the Age Discrimination in Employment Act, and that consequently the presumption of uniform usage throughout a statute should not be followed.

HHS determines that “an Exchange established by the State under section 1311 of the Patient Protection and Affordable Care Act is fully operational.” Thus, as part of an analysis of the §36B language, a court might examine whether the MOE language applies solely to state-created exchanges, or, also to federal-run exchanges. If the MOE requirements end only when a state-created exchange is fully operational, then a question may be raised whether the MOE requirements would continue indefinitely in a state that chose not to establish its own exchange, and whether that would be a result intended by Congress. An assessment of Congress’s intent regarding the application of the MOE requirements for state and federally-run exchanges might inform an analysis of the same language in the context of premium credits under §36B.

Administrative Authority to Interpret §36B to Include Federally Created Exchanges

As noted above, the Treasury Department, through the IRS, has issued final regulations that define an exchange, for purposes of §36B, to include both state and federally created exchanges. If these regulations were to be challenged as being outside the scope of the IRS’s authority under the Administrative Procedure Act,²² a determination of whether the Service exceeded its delegated authority in issuing the regulations under §36B may hinge on the degree of deference that a reviewing court accords the IRS’s understanding of the scope of its authority under ACA. Courts have traditionally “recognized that considerable weight should be accorded to an executive department’s construction of a statutory scheme it is entrusted to administer.”²³ However, whether a court will defer to a specific agency interpretation or implementation requires an application of the “familiar standards of review” established in *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*²⁴ In *Chevron*, the Supreme Court outlined what is largely considered a deferential test for reviewing an agency’s formal interpretation of its own authorizing statute or a statute it administers. At step one, a reviewing court must determine “whether Congress has directly spoken to the precise question at issue.”²⁵ If Congress has clearly addressed the issue, the court “must give effect to the unambiguously expressed intent of Congress.”²⁶ An agency interpretation that is contrary to the clear intent of Congress must be rejected. If, however, the court determines that Congress’s intent is unclear, or that the statutory language in question is ambiguous, the court proceeds to step two. At step two, a reviewing court will generally defer to any “permissible construction” of the pertinent statutory language.²⁷ This analysis is commonly referred to as the *Chevron* “two-step.”

Although *Chevron* is generally associated with judicial review of agency statutory interpretation, the analysis is “principally concerned with whether an agency has authority to act under a statute” and is used

²² The Administrative Procedure Act (APA) provides standards of judicial review that a court will use to determine whether an agency’s action is valid. 5 U.S.C. §§ 702, 704. For example, the APA provides that a reviewing court must set aside agency actions that are “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.” 5 U.S.C. § 706(2)(A). The APA also states that a reviewing court must “hold unlawful and set aside agency actions, findings, and conclusions found to be . . . in excess of statutory jurisdiction, authority, or limitations, or short of statutory right. 5 U.S.C. § 706(2)(C).

²³ *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.* 467 U.S. 837, 844 (1984).

²⁴ *Id.*; *Am. Library Ass’n v. FCC*, 406 F.3d 689, 698; *id.*

²⁵ *Chevron*, 467 U.S. at 842.

²⁶ *Id.* 842–43. (“If the intent of Congress is clear—that is the end of the matter, for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.”).

²⁷ *Id.* at 843. *See also* *Astrue v. Capato*, 566 U.S. ___, __ (2012) (deferring to the Social Security Administration’s longstanding interpretation in regulations issued after a notice-and-comment rulemaking and finding that the regulations “warrant the Court’s approbation” as they were “neither ‘arbitrary or capricious in substance, [n]or manifestly contrary to statute’” (quoting *Mayo Found. for Med. Ed. and Research v. United States*, 562 U.S. __ (2011); 131 S. Ct. 704 (2011)).

to discern “the boundaries of Congress’ delegation of authority.”²⁸ In 2001, the Supreme Court revisited *Chevron* and reinforced this point. In *United States v. Mead Corporation*, the Court held that an agency’s implementation of statutory authority “qualifies for *Chevron* deference when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority.”²⁹ *Mead* thus established a threshold requirement (what has been referred to as “step zero”³⁰) restricting *Chevron* deference to only formal rules and other interpretations holding the “force of law” and promulgated pursuant to delegated authority. Policy statements, agency manuals, and interpretive letters, on the other hand, generally do not warrant such deference.

Given this framework, the question of whether a reviewing court will defer to the Treasury Department’s interpretation of the scope of §36B will depend principally on whether that interpretation was made with the force of law pursuant to an exercise of delegated authority; whether the extent of that delegation was ambiguous; and whether the implemented interpretation was reasonable.

Action Taken Pursuant to Delegated Authority and with the Force of Law

The IRS has asserted that the “statutory language of section 36B and other provisions of the Affordable Care Act support the interpretation that credits are available to taxpayers who obtain coverage through a State Exchange, regional Exchange, subsidiary Exchange, and the Federally-facilitated Exchange.”³¹ In effect, the agency has interpreted the term “exchange” to encompass all forms of health exchanges envisioned by ACA. As previously noted, §36B generally provides, among other things, that taxpayers may receive a premium tax credit during a “coverage month” where they were “enrolled in through an Exchange established by the State under section 1311 of the Patient Protection and Affordable Care Act”³² Notably, §36B also provides the Secretary of the Treasury with broad authority to “prescribe such regulations as may be necessary to carry out the provisions of this section....”³³

Based on the reasoning of the *Mead* case, an agency’s implementation of a statutory provision qualifies for *Chevron* deference only “when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in the exercise of that authority.”³⁴ Under this broad language, it would appear that the IRS Rule would meet *Mead*’s preliminary threshold requirement. The IRS Rule was promulgated in the exercise of the broad authority delegated to the IRS to issue rules “necessary to carry out” §36B. Moreover, the Rule was adopted pursuant to notice and comment rulemaking and therefore clearly carries the “force of law.” In *Mead*, the Court noted that “congressional authorization to engage in the process of rulemaking” is a “very good indicator of delegation meriting *Chevron* treatment.”³⁵

²⁸ *Arent v. Shalala*, 70 F.3d 610, 615 (D.C. Cir. 1995).

²⁹ 533 U.S. 218, 226-27 (2001).

³⁰ See, e.g., Cass Sunstein, *Step Zero*, 92 Va. L. Rev. 187, 207 (2006).

³¹ Department of the Treasury, Internal Revenue Service, Health Insurance Premium Tax Credit, 77 Fed. Reg. 30377, 30378 (May 23, 2012).

³² 26 U.S.C. § 36B(c)(2).

³³ 26 U.S.C. § 36B(g).

³⁴ *Mead*, 533 U.S. at 226-27.

³⁵ *Id.* at 229. It should be noted that the *Mead* opinion has generated confusion among lower courts. The D.C. Circuit has issued a limited number of decisions that appear to more heavily scrutinize the threshold question of whether an agency was acting “pursuant to delegated authority.” See, *American Library Association et al. v. Federal Communications Commission*, 406 F.3d 689, 699 (D.C. Cir. 2005) (“The agency’s self-serving invocation of *Chevron* leaves out a crucial threshold consideration, i.e. (continued...)”).

The IRS Rule appears to be an exercise of the authority delegated to the agency to implement §36B, which includes the authority to provide refundable tax credits for taxpayers enrolled in a health insurance exchange. It may be argued that whether the scope of the IRS Rule was a proper interpretation of the statutory delegation, or specifically whether the agency misinterpreted the delegation by including tax credits for federally-facilitated exchanges in addition to state exchanges, is precisely the query the *Chevron* analysis was developed to address. This conclusion seems to be reaffirmed by the Supreme Court's recent decision in *Mayo Foundation for Medical Education & Research v. United States*,³⁶ where the Court evaluated the validity of regulations that prevented medical residents from being considered students for purposes of an exemption from Federal Insurance Contributions Act (FICA) taxes. The rules were issued pursuant to the Treasury Department's general authority to "prescribe all needful rules and regulations for the enforcement"³⁷ of the Internal Revenue Code. In finding it appropriate to evaluate the regulations under the *Chevron* analysis, the Court cited to *Mead* and noted that the Court indicated that its "inquiry in [this] regard does not turn on whether Congress's delegation of [rulemaking] authority was general or specific."³⁸

Step One: Whether Congress has Spoken to the Precise Question at Issue

If a reviewing court proceeds to the first step of the *Chevron* analysis, it will ask whether "Congress has spoken to the precise question at issue."³⁹ Thus, a court will consider whether Congress has clearly articulated a position on the breadth of the IRS's authority to provide premium tax credits for taxpayers enrolled in health insurance exchanges. The plain language of §36B suggests that premium tax credits are available only where a taxpayer is enrolled in an "Exchange established by the State." As noted previously, a strictly textual analysis of the plain meaning of the provision would likely lead to the conclusion that the IRS's authority to issue the premium tax credits is limited only to situations in which the taxpayer is enrolled in a state-established exchange. Therefore, an IRS interpretation that extended tax credits to those enrolled in federally facilitated exchanges would be contrary to clear congressional intent, receive no *Chevron* deference, and likely be deemed invalid. However, given the previously discussed alternative interpretive arguments that may suggest a more inclusive construction—including legislative history, legislative purpose, and context—a more searching analysis of Congress's intent in enacting the provision may lead to a less clear result.

As such, whether a court finds that there is sufficient ambiguity in §36B to proceed to *Chevron* step two may depend on the extent to which the court is willing to engage in a searching statutory interpretation involving text, context, legislative purpose, and legislative history, or whether the court would limit itself to a consideration of only the plain text of the provision.⁴⁰ In *Chevron* itself, the Supreme Court noted that a court should employ the "traditional tools of statutory construction" to "ascertain" whether

(...continued)

whether the agency acted pursuant to delegated authority."). However, in these cases the court has made clear that the rule in question would have failed under either *Chevron* "Step One" or "Step Two." See, *Aid Association for Lutherans v. United States Postal Service*, 321 F.3d 1166 (D.C. Cir. 2003) (holding that the Post Office had exceeded its delegated authority in broadly interpreting its authority under 39 U.S.C. 3626(j), but explaining that, "[o]ur judgment in this case is the same whether we analyze the agency's statutory interpretation under *Chevron* Step One or Step Two.").

³⁶ 131 S. Ct. 704 (2011).

³⁷ 26 U.S.C. § 7805(a).

³⁸ *Mayo Found. for Med. Educ. & Research v. United States*, 131 S. Ct. 704 at 713-14.

³⁹ *Chevron*, 467 U.S. at 842.

⁴⁰ This has been described as the "textualist-intentionalist divide." See generally, Linda Jellum, *Chevron's Demise: A Survey of Chevron from Infancy to Senescence*, 59 Admin. L. Rev. 725 (2007).

“congress had an intention on the precise question at issue.”⁴¹ The majority opinion then went on to consider text, purpose, and legislative history in concluding that the meaning of “stationary source” under the Clean Air Act was ambiguous.⁴² Justice Scalia, on the other hand, has led the opposition to the use of legislative history and legislative purpose at “Step One”, favoring a purely textualist approach to discerning whether a statute is ambiguous.⁴³

In a 2007 case potentially relevant to the instant situation, *Zuni Public School District No. 89 v. Department of Education*, the Supreme Court considered a situation in which the legislative history behind the provision seemed to suggest a congressional understanding contrary to the plain language of the statute.⁴⁴ In *Zuni*, the majority, invoking *Chevron*, upheld an interpretation by the Secretary of Education of the Impact Aid Act’s “equalization requirement” for aid expenditures to public school districts. Although the majority seemed to initially favor the textualist approach, noting that “normally neither the legislative history nor the reasonableness of the Secretary’s method would be determinative if the plain language of the statute unambiguously indicated that Congress sought to foreclose the Secretary’s interpretation,” the court then turned to legislative history and purpose “because of the technical nature of the language in question.”⁴⁵ Based on an evaluation of the statute’s history, the majority determined that Congress’s intent was unclear, and that the agency’s interpretation was reasonable. While the regulations in the *Zuni* case involved complex calculations, something that is arguably not analogous to the applicability of the premium tax credits in §36B, the case still arguably indicates Court’s willingness under certain circumstances to evaluate more than just the text of a statute in determining whether Congress has spoke on a particular issue.

Step Two: Whether the Agency Interpretation was Reasonable

As noted above, under “Step Two” of *Chevron*, if Congress has not directly spoken to the question at issue, the reviewing court’s role is limited to determining whether the agency’s interpretation was “based on a permissible construction of the statute.”⁴⁶ Where Congress has not clearly expressed its intent, a court “may not substitute its own construction of a statutory provision for a reasonable interpretation” of the agency.⁴⁷ Therefore, if Congress’s intent is unclear, the Court’s role at *Chevron* “Step Two” is generally to defer to any reasonable agency interpretation of the pertinent statutory language.⁴⁸ The Supreme Court has indicated that deference to an agency’s interpretation under step two is appropriate “whether or not it is the only possible interpretation or even one a court might think best.”⁴⁹ Thus, if a reviewing court determines that there is ambiguity surrounding the issue of whether premium credits are available in federal exchanges and reaches step two of the *Chevron* analysis with respect to the

⁴¹ *Chevron*, 467 U.S. at 843 n.9.

⁴² *Id.* at 862-65.

⁴³ Under Justice Scalia’s *Chevron* approach, the first step is simply to ask whether the enacted text is clear. Although initially following the intentionalist approach, some commentators have suggested that the majority of the Court now seems to generally support the textualist position. At least one commentator has asserted that “[t]oday, *Chevron*’s first step is routinely described and applied as a search for mere textual clarity.” Jellum, *supra* note 41, at 761.

⁴⁴ 550 U.S. 81 (2007).

⁴⁵ *Id.* at 90.

⁴⁶ *Chevron*, at 842-43.

⁴⁷ *Id.* at 844.

⁴⁸ *Id.* at 843.

⁴⁹ See, e.g., *Holder v. Gutierrez*, 566 U.S. __ (2012); 2012 U.S. LEXIS 3783, citing *Chevron*, 467 U.S. at 843-44.

regulations issued under §36B, the regulations will very likely be considered a reasonable agency interpretation of the statute and accorded deference by the court.⁵⁰

⁵⁰ See, Thomas J. Miles and Cass R. Sunstein, *Do Judges Make Regulatory Policy? An Empirical Investigation of Chevron*, 73 U. Chi. L. Rev. 823 (2006) (finding that more than 90 percent of invalidations under Chevron occurred at Step One).

Questions for the Honorable Douglas Shulman
Commissioner
Internal Revenue Service

Chairman Darrell Issa
Committee on Oversight and Government Reform
Hearing on "IRS: Enforcing ObamaCare's New Rules and Taxes"

Background for Questions 1-2

According to Nina Olson at the Taxpayer Advocate Service, "IRS to date has declined to include [Taxpayer Advocate Service] representatives on ACA implementation teams.... I am concerned that if the IRS excludes the 'voice of the taxpayer' from full participation in the implementation of the ACA, the risk of taxpayer and employer harm will be needlessly high."¹

- 1. Why hasn't IRS included Taxpayer Advocate Service representatives on ACA implementation teams?**
- 2. Does IRS plan to include Taxpayer Advocate Service representatives on ACA implementation teams moving forward?**

The leadership of the Affordable Care Act implementation effort and the National Taxpayer Advocate meet on a regular basis to discuss legal, policy and operational issues and concerns. These discussions include briefings on pending legal guidance and practical issues on a variety of provisions. This approach has been effective in identifying issues for further development during the guidance development process.

The implementation effort is currently working to more fully engage all of the operating units of the IRS – including the Taxpayer Advocate Service – in implementation as the effective date of the Exchange-related provisions approaches and the IRS moves toward detailed implementation planning, including customer service and compliance functions. The IRS is taking care to time the implementation planning to engage relevant operating functions in detailed planning at the appropriate time.

Background for Questions 3-5

In January, the Committee asked you for information regarding IRS's methods, aside from garnishing tax refund checks, to enforce the individual mandate. Your response indicated that IRS would "communicate with the taxpayer and attempt to resolve the outstanding liability."²

- 3. What will IRS communicate to taxpayers who owe the individual mandate tax penalty?**

¹ Olsen, Nina E. Testimony to the House, Committee on Oversight and Government Reform. *IRS' Enforcing Obamacare's New Rules and Taxes*, Hearing, August 2, 2012.

² Letter from Douglas Shulman to Darrell Issa, February 14, 2012.

4. How will IRS communicate that information to taxpayers?

5. If the penalty is not paid after IRS's communication, what other steps will IRS take to enforce payment?

The individual responsibility provision, IRC section 5000A, will be a part of the normal annual Form 1040 filing cycle. For most taxpayers, they will merely indicate the fact of coverage and have no further interaction with the IRS on the topic. For a taxpayer who has a section 5000A liability, it would be only one element of the return and the particular taxpayer may have an overall refund or an overall liability depending on all elements of the return taken together.

Most taxpayers are highly compliant. When they have a net tax liability, they make a payment with their return. For those who do not remit payment with their return, the IRS will communicate with the taxpayer through the mail and attempt to resolve the outstanding liability. Such correspondence will explain the reasons for the contact and explain the taxpayer's obligations and options. A substantial majority of IRS collection revenue comes during this notice process.

If after correspondence there remains a balance due, that balance remains on the taxpayer's account until satisfied, whether through later payment by the taxpayer or by refund offset in a future year. For a liability attributable to section 5000A, the statute prohibits other IRS enforcement actions, such as filing notices of federal tax liens and levies.

Background for Questions 6-8

The Patient Protection and Affordable Care Act (PPACA) establishes a new definition of income - household income - for tax purposes. Please provide information on the following:

6. According to tax lawyer Dan Pilla, "Under current law, there is no requirement to report household income to the IRS. Thus, there are no rules for figuring it and no mechanism for reporting it"³ Is that true? If your answer is no, please explain.

No. For the vast majority of taxpayers, the data necessary to compute household income is already reported on the annual Form 1040 or is easily derived from existing line items.

The definition of "household income" is outlined in the statute itself. Household income is defined by section 36B(d)(2) of the Code as the modified adjusted gross income of all individuals included in the taxpayer's "family size" who are required to file an income tax return. A taxpayer's "family size" consists of the individuals for whom the taxpayer claims a personal exemption deduction for the taxable year. Modified adjusted gross income means adjusted gross income increased by amounts excluded from gross income

³ Tax Freedom Institute, Inc., *Implementing National Health Care*, Available at: <http://taxfreedominstitute.com/implementing-national-health-care.html>.

under section 911 of the Code, tax-exempt interest a taxpayer receives or accrues during the taxable year, and an amount equal to the portion of the taxpayer's social security benefits not included in gross income for the taxable year.

- 7. According to Mr. Pilla, "Substantial changes will have to be made to tax forms and instructions and the IRS will have to reprogram its systems to accept, store, retrieve and utilize the information."⁴ Is that true? If your answer is no, please explain.**

Every time the tax law is amended, the IRS analyzes what forms and systems need to be adjusted to accommodate the legislative change and educate and support the tax filing public. For the Affordable Care Act, such analyses are ongoing and steps are being taken to ensure that the relevant information is available for the public for each provision.

- 8. How will people calculate household income? What information must be reported, and what factors must be considered?**

The statute defines household income, as explained in the response to Question 6.

- 9. Suppose I owe a \$1,000 tax penalty from the individual mandate, and I refuse to pay it. Is there anything to prevent the IRS from deeming the first \$1,000 of my income-tax withholding to be payment of my mandate penalty, and then using fines, liens, and/or seizures to collect the \$1,000 I now owe in income taxes? If you answer yes, please explain.**

Section 5000A(g)(2)(B) provides that, notwithstanding any other provision of law, the Secretary of the Treasury shall not file a notice of lien with respect to any property of a taxpayer by reason of any failure to pay the penalty imposed by section 5000A, or levy on that property with respect to any failure to pay.

Under Section 31(a) of the Internal Revenue Code and the related regulations (which are unrelated to the Affordable Care Act), the IRS cannot circumvent the prohibitions contained in Section 5000A(g)(2)(B) by applying an individual's wage withholdings to an outstanding Section 5000A penalty before applying such withholdings to an individual's income tax liability.

- 10. Since Obamacare's employer mandate penalty is "assessable" in the same manner as other employment tax penalties, is it true that IRS does not have to offer the employer an opportunity to review and contest the determination prior to assessing the penalty?**

- 11. Is it true that any appeals of the employer mandate come into play only after assessment and collection begins?**

⁴ *Id*

Section 4980H(d) provides, in part, that any assessable payment shall be collected in the same manner as an assessable penalty under chapter 68, subchapter B. Subchapter B covers a wide variety of assessable penalties, unrelated to “employment tax penalties” referenced in the question. The assessable penalties under Subchapter B are quite varied, and over the years the IRS has developed administrative appeals tailored to particular settings and taxpayer types.

For section 4980H, some stakeholders have requested that the IRS provide a procedure under which the IRS would correspond with the employer prior to the notice contemplated by the statute, to ensure the best information is available before a penalty is assessed. The IRS is actively considering this possibility. In addition, the employer would have all the administrative and statutory appeal procedures normally available for assessable penalties. Finally, some employers have requested a procedure to self-assess the penalty where they know that they will owe it. IRS is considering that option as well.

Background for Question 12

The American Recovery and Reinvestment Act of 2009 amended the Hope Scholarship Tax Credit to provide for a refundable tax credit known as the American Opportunity Tax Credit (AOTC).⁵ The Treasury Inspector General for Tax Administration (TIGTA) identified 2.1 million individuals erroneously receiving \$3.2 billion in education credits in 2010.⁶ This was out of \$18 billion in total education credits received by 12 million individuals as of 2010.⁷ TIGTA found that many people had claimed education credits by mistake, because the eligibility requirements had not been made clear by IRS.⁸

12. Why was there such a high error rate with the AOTC in 2010? Did IRS learn any lessons from the significant problems it had administering the AOTC?

The majority of the estimated errors in TIGTA's report are based on the inability to match tax returns claiming the credit with a corresponding Form 1098-T, *Tuition Statement*, required to be filed by educational institutions with the IRS by the end of March during the filing season. While the form is a key source to determine eligibility for the credit, its absence or the absence of certain information on it does not necessarily mean that a taxpayer is not eligible for the AOTC. The law does not disqualify taxpayers from claiming the credit if the educational institution has not complied with its reporting requirements. In fact, TIGTA reported on compliance issues around information returns like Tuition Statements in their AOTC and other audits. Finally, some expenditures (e.g., course materials) contribute to AOTC eligibility but are not reported on the Form 1098-T.

We are working with educational institutions and other outside stakeholders to ensure that Form 1098-T reporting is accurate. We are also revising the reporting requirements

⁵ George J. Russell Testimony to the House, Committee on Ways and Means Subcommittee on Oversight. *Improper Payments in the Administration of Refundable Tax Credits*. Hearing, May 25, 2011.

⁶ Treasury Inspector General for Tax Administration. *Recovery Act: Millions of Dollars in Education Credits Appear to be Erroneous*, Report, September 16, 2011. Available at <http://www.recovery.gov/Accountability/inspectors/Documents/201141083fr.pdf>

⁷ *Id.*

⁸ *Id.*

and tax forms so that the IRS receives the information required to assess who legitimately qualifies for AOTC. For tax year 2012 we are revising Form 8863, *Education Credits (American Opportunity and Lifetime Learning Credits)*, on which the AOTC is claimed. Taxpayers claiming the AOTC will be required to identify the school they attended and answer new eligibility questions before filing and claiming the credit.

Although the IRS disagreed with the level of error estimated in TIGTA's findings, we are using lessons learned from administering all the individual refundable credits to improve both our educational and compliance strategies around AOTC. We continue to strive to provide a balanced program, applying safeguards and controls to deter payment of improper claims without adversely impacting timely payment to taxpayers who are entitled to the AOTC. We are reviewing AOTC claims in our document matching program to focus on taxpayers who claimed the credit but did not have a Form 1098-T document supporting the credit. We developed new filters to identify and follow up with students, based on their characteristics, who are clearly not in post-secondary education and, therefore, not eligible to claim the AOTC. We are looking into possible alternatives to address return preparers who may be involved with AOTC noncompliance.

Background for Question 13 - 18

IRS issued a final rule on May 18, 2012, that extended eligibility for tax credits and cost-sharing subsidies to individuals who purchase qualifying insurance plans in federally run Exchanges.⁹ According to a recent CRS analysis:

The plain language of Section 36B suggests that premium tax credits are available only where a taxpayer is enrolled in an "Exchange established by the State." As noted previously, a strictly textual analysis of the plain meaning of the provision would likely lead to the conclusion that the IRS's authority to issue the premium tax credits is limited only to situations in which the taxpayer is enrolled in a state established exchange. Therefore, an IRS interpretation that extended tax credits to those enrolled in federally facilitated exchanges would be contrary to clear congressional intent ... and likely be deemed invalid.¹⁰

- 13. Could IRS have simply implemented the statutory language as it was written, with individuals purchasing coverage in federal exchanges ineligible for PPACA's tax credits and cost sharing subsidies? If you answer no, please explain.**
- 14. In promulgating the rule, the IRS said that "the statutory language ... supports the interpretation" that tax credits are available in federal exchanges. You reiterated these claims at The Committee's hearing on August 2, 2012. Please identify the specific statutory provision(s) that authorize the IRS to grant tax credits in federal exchanges.**

⁹ Department of the Treasury: Internal Revenue Service, Final Regulation" 63 Federal Register 100 (23 May 2012), pp. 30377.

Available at: <http://www.gpo.gov/fdsy/pkg/FR-2012-05-23/pdf/2012-12421.pdf>.

¹⁰ Jennifer Staman and Todd Garvey, Legal Analysis of Availability of Premium Tax Credits in State and Federally Created Exchanges Pursuant to the Affordable Care Act, Congressional Research Service Memorandum. July 23, 2012.

15. Does the information-reporting requirement in Section 36B(f) contain any language authorizing tax credits in Exchanges established by the federal government under Section 1321? If you answer yes, please provide the specific language in Section 1321.
16. Did IRS have any communications with anyone outside of IRS about whether this rule should provide tax credits in federal Exchanges? If so, who did IRS communicate with, and what was the nature of those communications?
17. Does the information-reporting requirement in 36B(f) conflict in any way with how 36B(b) and (c) limit tax credits to state-created Exchanges?
18. In promulgating the rule, the IRS said that “the relevant legislative history does not demonstrate that Congress intended to limit the premium tax credit to State Exchanges.” Please provide the relevant legislative history that demonstrates that Congress intended individuals who purchase insurance in exchanges established by the federal government to qualify for PPACA’s tax credits.

Questions 13-18 are addressed in the attached October 12, 2012 letter from the Department of the Treasury to Chairman Issa, which is in response to the August 20, 2012 Committee letter to IRS Commissioner Douglas H. Shulman.

Background for Question 19

In your testimony before the Committee, you stated that “the IRS is continuing its long tradition of being a nonpartisan agency that implements the laws that Congress passes.” In your written testimony, you discussed the enormous postcard outreach effort that IRS conducted to advertise the PPACA’s small business tax credits. However, in response to the Chairman’s question, you stated that IRS does not plan on sending postcards to businesses about any of the law’s 20 tax increases.

19. Please explain why IRS decided to conduct a massive postcard outreach with respect to the law’s small business tax credits, but not a similar effort with respect to the law’s many tax increases.

Whenever there is new legislation, the IRS assesses numerous tools for educating the public about new responsibilities or benefits. A plan is tailored to the type of provision, the ability to timely reach the intended audience, whether normal annual processes would be likely to achieve the goals, and feedback from the community. In this particular case, the credit was enacted mid-year with a retroactive effective date, such that many small businesses risked not being aware of this new incentive. After evaluating the available data sources, the IRS conducted broad-based outreach to small businesses because there was little data available that would support better targeting of outreach (e.g., which small businesses offer health coverage to their employees). The IRS conducted a much larger outreach initiative in 2008, when it sent special mailings to taxpayers who may be eligible for a special economic stimulus payment. These types of special outreach efforts

are not generally needed for tax law changes that come into effect with a prospective effective date, where there is sufficient time for IRS to work with practitioners and other stakeholder groups to ensure that taxpayers have the information that they need.

20. HHS has issued a final rule that requires a taxpayer enrolled in a qualified health plan through a state Exchange to report certain changes in household income within 30 days.¹¹ Will IRS have a role in enforcing this rule? If so, please explain what IRS's enforcement role will be?

IRS does not have a role in enforcing that rule.

21. In your testimony before the Committee, you testified that the IRS Office of Data Privacy and Security “will go out and do audits to make sure it is right.” Are you referring to audits that will be conducted for insurance exchanges established in the state? What specifically will an exchange have to demonstrate in order to receive confidential taxpayer information from IRS?

The IRS takes protection of taxpayer information very seriously. Section 6103 of the Code provides that no federal tax information (FTI) may be furnished by the IRS to another agency unless the other agency establishes physical, administrative, and technical safeguards for protecting the return information it receives. Thus, disclosure of tax information to other agencies is conditioned on the recipient agency maintaining a secure place for storing the information, restricting access to the information to people to whom disclosure can be made under the law, providing other safeguards necessary to keep the information confidential, and returning or destroying the information when the agency is finished with it. The IRS Office of Safeguards is responsible for enforcing these requirements for FTI maintained outside the IRS by other federal and state agencies and their contractors. See IRS Publication 1075 “Tax Information Security Guidelines for Federal, State and Local Agencies.”

To demonstrate compliance, agencies that are authorized to receive tax data must file a Safeguard Procedures Report (SPR) with the IRS. The SPR covers the management, operational and technical controls for information systems and how FTI will be protected from unauthorized disclosure or use. IRS will approve a state’s SPR and notify HHS of such approval before any FTI will be released by HHS to a state entity for authorized use in the eligibility and enrollment process. IRS reviews generally include an on-site evaluation of the use of FTI and the measures employed by the state to protect the data, which includes scanning systems, interviewing employees, performing information technology scans and documenting findings.

IRS is working closely with HHS and states to assist in the completion of the SPR and to provide technical and operational guidance on how to incorporate the full range of IRS requirements in systems handling FTI. IRS has also worked closely with HHS to ensure

¹¹ US Department of Health and Human Services, Patient Protection and Affordable Care Act: Establishment of Exchanges and Qualified Health Plans: Exchange Standards for Employers, 75 CFR 155-57, § 155.330 (2012).

that IRS Publication 1075 “Tax Information Security Guidelines for Federal, State and Local Agencies” requirements are incorporated in Exchange regulations, minimum data security standards, and the HHS state Exchange certification process.

Questions for The Honorable Douglas Shulman
Commissioner
Internal Revenue Service

Representative Todd Platts
Committee on Oversight and Government Reform

Hearing on "IRS: Enforcing ObamaCare's New Rules and Taxes"

Providing taxpayer assistance is an important part of IRS's role. However, IRS's goal level of customer service has significantly dropped in the last few years, down to 61 percent in 2012.

1. **What resources does IRS currently have to provide taxpayer assistance? Please include expenses and the number of Full Time Employees (FTEs).**
2. **How many FTEs is IRS adding or planning to add to assist the public with the provisions of the Patient Protection and Affordable Care Act (PPACA)?**
3. **How will IRS manage calls that cannot be resolved within the agency, for instance, calls that require consultation with HHS or state exchanges?**
4. **Is IRS making contingency plans in case more assistance is needed than it has prepared for?**

The FY 2012 enacted appropriation for the IRS provided \$2.2 billion for Taxpayer Services - \$632 million and 5,862 FTE for Pre-filing Taxpayer Assistance & Education, which includes the Taxpayer Advocate Service, and \$1,607 million and 24,673 FTE for Filing and Account Services, which includes funding for the Customer Service Representatives on the phones.

HHS and the Exchanges will be the primary sources of information and assistance for individuals seeking health care information. Exchanges will be the go-to source for assistance with eligibility and enrollment and changes in circumstance beginning with open enrollment in October of 2013. IRS is currently in the planning stages about how, and when, to integrate the Exchange-related Affordable Care Act tax law topics that will come up during the 2015 tax filing season. The IRS is collaborating with HHS to provide user-friendly customer support options across the agencies.

5. **What information will IRS share with HHS? What information will IRS share with state insurance exchanges?**

Section 6103(l)(21) of the Code permits the disclosure of federal tax information (FTI) first, by the IRS to HHS, second, by HHS to Exchanges and state agencies that administer Medicaid and CHIP programs, and then third, by Exchanges to applicants as part of the enrollment process. Thus, the FTI will flow from IRS to HHS and then the same

information will flow from HHS to Exchanges; no data will flow directly from IRS to Exchanges. IRS will disclose available items of return information to HHS after an individual submits an application for financial assistance in obtaining health coverage to an Exchange or State agencies that administer Medicaid, CHIP, or basic health plans.

Section 6103(l)(21)(A) authorizes the release of the following taxpayer information: “(i) taxpayer identity information with respect to such taxpayer, (ii) the filing status of such taxpayer, (iii) the number of individuals for whom a deduction is allowed under section 151 with respect to the taxpayer (including the taxpayer and the taxpayer’s spouse), (iv) the modified adjusted gross income (as defined in section 36B) of such taxpayer and each of the other individuals included under clause (iii) who are required to file a return of tax imposed by chapter 1 for the taxable year, (v) such other information as prescribed by the Secretary by regulation to indicate whether the taxpayer is eligible for such credit or reduction (and the amount thereof), and (vi) the taxable year with respect to which the preceding information relates or, if applicable, the fact that such information is not available.”

The IRS is also proposing to provide coding to help states understand the information being provided. These additional coding data elements were included in an NPRM dated April 30, 2012: see Federal Register, vol. 77, no. 83 (77 FR 25378).

6. How will IRS secure this information and prevent it from being misused or accidentally leaked?

The IRS takes protection of taxpayer information very seriously. Section 6103 of the Code provides that no federal tax information (FTI) may be furnished by the IRS to another agency unless the other agency establishes physical, administrative, and technical safeguards for protecting the return information it receives. Thus, disclosure of tax information to other agencies is conditioned on the recipient agency maintaining a secure place for storing the information, restricting access to the information to people to whom disclosure can be made under the law, providing other safeguards necessary to keep the information confidential, and returning or destroying the information when the agency is finished with it. The IRS Office of Safeguards is responsible for enforcing these requirements for FTI maintained outside the IRS by other federal and state agencies and their contractors.

To demonstrate compliance, agencies that are authorized to receive tax data must file a Safeguard Procedures Report (SPR) with the IRS. The SPR covers the management, operational and technical controls for information systems and how FTI will be protected from unauthorized disclosure or use. IRS will independently approve a state’s SPR and notify HHS of such approval before any FTI will be released by HHS to a state entity for authorized use in the eligibility and enrollment process. IRS reviews generally include an on-site evaluation of the use of FTI and the measures employed by the state to protect the data, which includes scanning systems, interviewing employees, performing information technology scans and documenting findings.

IRS is working closely with HHS and states to assist in the completion of the SPR and to provide technical and operational guidance on how to incorporate the full range of IRS requirements in systems handling FTL. IRS has also worked closely with HHS to ensure that IRS Publication 1075 Tax Information Security Guidelines for Federal, State and Local Agencies, requirements are incorporated in Exchange regulations, minimum data security standards and guidance and the HHS state Exchange certification process.

7. Has IRS taken any action to address the deficiencies noted in GAO's report? If yes, please detail actions taken. If not, does IRS have plans to address GAO's concerns?

Yes, the IRS has taken actions to address the issues raised by GAO as part of our ongoing implementation planning and analysis. In particular, the IRS has undertaken a substantial effort to update its implementation costs estimates. The report itself acknowledges that when the IRS completes its corrective actions later this year it will have addressed the issue.

8. What does IRS estimate will be the total cost to implement PPACA between now and FY 2014? How much does IRS estimate it will cost to administer PPACA provisions annually after FY 2014?

The IRS's 2013 budget submission includes \$360 million for implementing the tax law provisions of the ACA. The IRS is currently in the process of formulating the FY 2014 budget request.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

OCT 12 2012

The Honorable Darrell Issa
Chairman
Committee on Oversight and Government Reform
U.S. House of Representatives
Washington, DC 20515

Dear Chairman Issa:

I am writing in response to your recent letter to Commissioner Shulman regarding section 36B of the Internal Revenue Code (Code). I am responding on his behalf because your letter raises important issues regarding tax policy, the standard process by which Treasury regulations are developed collaboratively between the Department of the Treasury's Office of Tax Policy (OTP) and the IRS, and communications between the IRS and OTP regarding the proposed and final section 36B regulations promulgated by Treasury.

More specifically, your letter raises questions about whether taxpayers who purchase health insurance through exchanges operated by the federal government (federally-facilitated exchanges) are eligible for the premium tax credit under section 36B of the Code. Let me assure you that we take seriously our responsibility to implement the tax laws passed by Congress. We do so in a careful and thoughtful way, with the goal of implementing the law consistent with congressional intent and resolving any statutory ambiguities in a reasonable manner that gives effect to the purpose of the statute.

As you know, Section 36B(b)(2)(A) provides that the amount of the premium tax credit is based on the premiums for one or more qualified health plans in which a taxpayer enrolls through an "Exchange established by the State under section 1311" of the Affordable Care Act (ACA). ACA section 1311(d)(1) provides that "[a]n Exchange shall be a governmental agency or a nonprofit entity that is established by a State." Under ACA section 1321(c), if a state chooses not to establish an exchange or will not have an exchange in operation by January 1, 2014, the Secretary of Health and Human Services (HHS) "shall . . . establish and operate such Exchange within the State" to serve the residents of that state.

Treasury regulations implementing section 36B provide that individuals who enroll in coverage through a federally-facilitated exchange are eligible for premium tax credits. Treasury and the IRS developed these regulations in accordance with our standard process for drafting, approving, and publishing tax regulations. The process begins with the IRS Office of Chief Counsel. IRS lawyers review the particular statute to identify any issues that regulations should address and to develop preliminary resolutions of those issues. The IRS lawyers apply well-established principles of statutory construction and draw on their long experience implementing the Code. The analysis is then shared with OTP tax lawyers, and the two groups confer about the proper

interpretation of the statute, discuss any differences of opinion, and develop a consensus approach.

Under this standard procedure, OTP and IRS lawyers work together to draft a Notice of Proposed Rulemaking, which is published in the Federal Register. Treasury solicits public comments on the proposed regulations during an official comment period; and, in many cases, the IRS also holds a public hearing to allow stakeholders to provide feedback in person. IRS and OTP lawyers review any comments they receive and consider whether any of the suggested changes should be adopted. Last, IRS and OTP lawyers draft a final regulation, which includes responses to any comments and makes modifications to the proposed regulations as necessary. All final tax regulations are signed by both the IRS Deputy Commissioner for Services and Enforcement and the Treasury Assistant Secretary for Tax Policy.

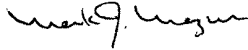
The IRS and OTP followed this standard procedure in developing the proposed and final regulations under section 36B. In particular, first the IRS, and then the OTP lawyers considered the express language of section 36B, as well as other relevant provisions of the ACA. They separately and together concluded that the ACA should be interpreted to provide tax credits to individuals enrolling through all exchanges, whether directly operated by a state government or federally-facilitated. This approach was reflected in proposed regulations issued in August 2011. We received numerous written and oral comments in response to the proposed regulations – some of which were supportive; others argued for a different interpretation. The IRS and OTP reviewed the issue again, taking into account the numerous comments, and concluded the statute should be interpreted as in the proposed regulations. Treasury published final regulations in May 2012 that adopted this view.

Your letter inquires about the legal basis for Treasury's position. We interpreted the statutory language in context and consistent with the purpose and structure of the statute as a whole, pursuant to longstanding and well-established principles of statutory construction. For example, ACA section 1311 refers to an exchange being "established by a State." Congress provided in section 1321, however, that where a state was not proceeding with an exchange, HHS would establish and operate "*such* Exchange within the State," making a federally-facilitated exchange the equivalent of a state exchange in all functional respects. Moreover, throughout the ACA, Congress refers to the exchanges as "exchanges," "exchanges established by a state," and "exchanges established under the ACA." There is no discernible pattern that suggests Congress intended the particular language in section 36B(b)(2)(A) to limit the availability of the tax credit.

In addition, the information reporting requirements of section 36B(f)(3) apply to exchanges under both ACA sections 1311 and 1321. This requirement relates to administration of the premium tax credit. The placement of this provision in section 36B and the information required to be reported – including information related to eligibility for the credit and receipt of advance payments – strongly suggests that all taxpayers who enroll in qualified health plans, either through the federally-facilitated exchange or a state exchange, should qualify for the premium tax credit. Our interpretation is consistent with the explanation of the ACA released by the non-partisan Congressional Joint Committee on Taxation and with the assumptions made by the Congressional Budget Office in estimating the effects of the ACA.

Finally, we have enclosed documents responsive to your requests. Please let us know if you need additional information. We hope this is helpful and we look forward to working with you in the future.

Sincerely,

A handwritten signature in black ink, appearing to read "Mark J. Mazur". The signature is fluid and cursive, with the first name "Mark" being more prominent.

Mark J. Mazur
Assistant Secretary (Tax Policy)

Enclosures